REVIEW OF INTERNATIONAL AVIATION POLICY AND BILATERAL AGREEMENTS

(101-78)

HEARING

BEFORE THE

SUBCOMMITTEE ON AVIATION

OF THE

COMMITTEE ON
PUBLIC WORKS AND TRANSPORTATION
HOUSE OF REPRESENTATIVES

ONE HUNDRED FIRST CONGRESS

SECOND SESSION

OCTOBER 11, 1990

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SUBCOMMITTEE ON AVIATION

hearing on

REVIEW OF U.S. INTERNATIONAL AVIATION POLICY AND BILATERAL NEGOTIATIONS

Thursday, October 11, 1990
9:30 a.m.

SUMMARY OF SUBJECT MATTER

The hearing will receive testimony as part of a comprehensive review of U.S. international civil aviation policy and bilateral negotiations. On Thursday, October 11, the Subcommittee will receive testimony from U.S. Department of Transportation witnesses. At a later date, testimony from other interested parties and organizations will be taken.

The International Civil Aviation Framework

Since World War II and the 1944 Chicago Convention on International Civil Aviation, civil aviation relationships have largely been governed by bilateral agreements between governments. It was decided then that issues of how much air service, by how many airlines, and under what pricing and marketing arrangements would be negotiated and resolved through government-to-government bilateral agreements. The Chicago Convention is a relatively unique agreement in that other sectors of the global economy do not operate under such a regime of governmental bilateral agreements.

The U.S. has entered into 72 bilateral civil aviation agreements with other countries. There are some instances of multinational arrangements, but these are very limited and specific such as an agreement encompassing the three Scandinavian countries. As the European Community moves toward its 1992 economic integration, the U.S. may eventually negotiate multilaterally with the European Community, but for the near future, the bilateral approach will continue to be the mechanism by which aviation issues are resolved between nations.

One important aspect of the bilateral system, at least from the U.S. standpoint, is that the rights and benefits exchanged through these bilaterals are limited to civil aviation matters. Other sectors hardly ever enter the picture. In other words, fishing rights are not exchanged for aircraft landing rights; landing rights are exchanged for landing rights or other aviation opportunities.

Bilateral civil air negotiations between the U.S. and its major civil aviation partners take place with relative frequency. Talks to resolve issues and problems can take place three or four times a year with countries such as the United Kingdom or Japan. Talks between the U.S. and smaller partners may occur once a year or less frequently.

U.S. civil aviation negotiation teams are typically composed of representatives from the Departments of State and Transportation. The State Department usually leads the negotiations with the Department of Transportation providing the policy guidance.

Negotiations are usually prompted by the wish of the airlines of either or both countries to expand or change service, fly to a new city, or make changes in fares. But talks also take place to resolve disputes and problems involving "doing business" issues, which are the more mundane, but often very important, aspects of the air transportation business. These include how and who will handle aircraft when on the ground in a foreign country, how tickets will be marketed and sold, customs regulations on cargo, currency transactions, landing fees, and the availability of adequate airport space to conduct operations. Also, access of U.S. airline computer reservation systems to foreign markets has become a major topic in some civil air talks, particularly with European and Asian governments.

Bilateral agreements typically provide formal mechanisms to resolve disputes, complaints and problems when negotiations fail. Also, the International Air Transportation Competition Act and the Fair Competitive Practices Act provide procedures whereby anti-competitive practices of foreign carriers or foreign governments are investigated by the U.S.

Department of Transportation with follow up action by the DOT within specified periods of time.

U.S. International Aviation Policy

Since the late 1970s, the policy and approach of the U.S. Government with respect to civil air relations has been to negotiate bilateral civil air agreement that seek to establish a framework in which the airlines can provide services with a minimum of U.S. and foreign government approvals, interference, and restrictions. The pro-competition policies of the U.S. Government became law in 1980 upon enactment of the International Air Transportation Competition Act.

A major cornerstone of U.S. policy since the Carter Administration has been to encourage competition and low fares by removing governments, both U.S. and foreign, from decision-making on what airline fares in particular markets should be. When this type of arrangement has been agreed upon, discount fares in these markets have usually become more prevalent. In the absence of this type of arrangement fares are typically higher because foreign governments have typically wanted to keep their countries' airlines protected from price competition.

The U.S. pro-competitive approach to civil air relations has met with varying degrees of success from country to country, but there are only a handful of bilateral agreements with the major aviation partners that could be described as truly competitive arrangements. Though relatively good price competition has developed between the U.S. and some European countries, the rest of the world remains quite regulated with respect to fares causing fares to be relatively high.

Though a pro-competitive approach remains the overarching goal of U.S. policy, in recent years U.S. civil aviation negotiators have placed increasing emphasis on ensuring that balanced deals are achieved when new route rights are exchanged and on resolving the ubiquitous "doing business" problems afflicting U.S. airlines in many foreign countries.

Early this year, DOT policy makers sought to reinvigorate the pro competition approach to international aviation. The U.S. government proposed to the United Kingdom, France and Germany that "open skies" be declared between the U.S. and these countries. The U.S. proposed unrestricted rights or routes between these countries and the U.S. with pricing and scheduling governed only by market forces. The three countries have not taken the U.S. up on the proposal.

U.S. aviation policy makers are also increasingly talking of the need to start thinking about negotiating multilaterally, particularly with Europe, in order that the full market potential of the world's aviation system be exploited. U.S. policy makers believe that the bilateral framework is constricting air carriers' abilities to provide all the service the traveling public needs and is demanding. They believe that a regional or multilateral approach could better serve the needs of the traveling public air carriers by removing barriers and restrictions that exist in the bilateral system.

Typical of the barriers under the bilateral system are limits on the number of carriers that can serve a market, the number and timing of flights, and the ability of carriers to serve markets beyond the gateway. By eliminating these barriers the government framework would be brought in line with the market realities of the increasingly global aviation system. Informal discussions have been initiated with the aviation staff of the European Commission, but the authority of the Commission is not clear at this point.

In a further effort to move toward a more open and liberal international aviation system, the DOT announced earlier this year a new policy of permitting foreign carriers to serve U.S. points under certain circumstance without obtaining the rights through a traditional bilateral negotiation. If a foreign carrier seeks to start scheduled service between its country and a U.S. point and no other airline is providing service in that market, and the bilateral agreement is competitive, liberal, and free of dispute, the U.S. will permit that service to start without seeking rights in return. Netherlands/Baltimore service by KLM, Switzerland/Philadelphia service by Swissair, Chile/Washington service by Ladeco, and Frankfurt/ Charlotte services by Lufthansa have been approved under this arrangement. Observers expect new foreign carrier service to the U.S. to expand under this new arrangement as U.S. cities will actively solicit foreign carrier service.

Finally, two fundamental legal principles governing U.S. international aviation policy should be noted because these legal principles will increasingly be the subject of discussion and debate over aviation policy. First, the Federal Aviation Act requires that U.S. airlines be controlled, with at least 75% of the voting stock owned, by U.S. citizens. The primary reason for this is to ensure that airlines, which may be needed to serve the national security interests of the U.S., are in the hands of U.S. citizens.

The second fundamental principle is that all nations, including the U.S., prohibit what is termed 'cabotage,' a centuries old concept originating in the maritime sector. Cabotage is the carriage of passengers and goods between two domestic points by a foreign carrier. All nations have reserved for their domestic carriers, for reasons ranging from national security to protection of domestic industries, the right to carry domestic traffic.

However, cabotage is increasingly being discussed in the international aviation community. From time to time, in recent years, foreign governments have expressed an interest in exchanging cabotage rights with the U.S. Also, the U.S. Government has recently been presented with ownership and marketing arrangements between U.S. and foreign carriers that have raised questions of whether the arrangements' practical effect amounted to cabotage.

The U.S. Government's policy to date has been to oppose cabotage within the United States because U.S. domestic markets are disproportionately large compared to other countries' domestic markets. There is nothing of equal value in any foreign country's domestic markets to the large U.S. domestic markets, hence no trade of bilateral cabotage rights has been worth entering into from the U.S. perspective. The largest domestic markets within the United Kingdom, for example, pale next to the large U.S. domestic markets in both size and revenues. However, limited forms of cabotage for foreign carriers are increasingly being considered particularly in the case of Canada (to be discussed in more detail later). Integration of the European Economic Community may also challenge the cabotage principal.

Passenger Travel Between the U.S. and Other Countries

In 1989, approximately 74 million passengers traveled between the United States and other countries. Forecasts for 1990 anticipate 78-79 million passengers. International boardings account for 8% of the total boardings on U.S. airlines.

International passenger traffic between the U.S. and the rest of the world has enjoyed strong and healthy growth since the late 1970s. Since 1976, when approximately 33 million airline passengers flew between the U.S. and other countries, there has been more than a doubling of traffic. In some regions, the traffic growth has been even more pronounced. Travel between the U.S. and the Far East has climbed from approximately 3 million passengers in 1976 to approximately 11.5 million today, a 3 1/2 fold increase.

Until 1988, the U.S. carriers' market share was historically in the 48-49% range. In 1988, U.S. market share climbed to 52%; held there in 1989; and so far this year has climbed into the 53-54% range. Not only has the international passenger market expanded, but so has the U.S. carrier share of it.

Of the 74 million traveling between the U.S. and other countries in 1989, 56% were U.S. citizens. The vast preponderance of international travelers (95%) use scheduled flights while only 5% fly charter services.

The following table provides passenger traffic data for the U.S. international markets that had more than one million passengers in 1989.

Passenger Travel Between the U.S. and Other Countries

(Calendar Year 1989)

Country	Passenger Traffic in Millions	% U.S. Citizens	% on U.S. Flag Airlines
Canada	13.0	N/A	66
United Kingdom	9.2	50	51
Japan	8.2	24	55
Mexico	7.5	72	55
Germany-West	4.2	57	51
France	3.1	55	64
Bahama Islands	2.9	75	74
Dominican Republic	1.8	77	77
Jamaica	1.8	72	38
Netherlands	1.5	49	14
Italy	1.4	62	54
Switzerland	1.3	59	36
Scandinavia	1.2	38	45
Korea-South	1.2	56	34
Netherland Antilles	1.1	82	79

Committee staff has data for other countries for those who are interested.

The Federal Aviation Administration forecasts that international passenger enplanements will grow at an average annual rate of 5.4% for the balance of the century which would put total travelers between the U.S. and other countries at approximately 120 million at the turn of the century. The rate of forecasted growth varies considerably among world regions. While traffic between the U.S. and Europe and Latin America is expected to grow annually at 4.4% and 4.3% respectively, travel between the U.S. and Pacific countries is anticipated to grow an average of 9% annually.

It should be noted that the accuracy of long range forecasting of international air traffic patterns and growth is often problematic. For example, in recent years, traffic growth, particularly in the Pacific, has exceeded expectations. On the other hand, international events, particularly terrorist activity, can seriously dampen international traffic very quickly and unexpectedly, as was the case in 1986.

International Air Cargo

The shipment of air cargo or freight has increased significantly in its importance within the U.S. international aviation sector. In 1989, U.S. carrier international freight revenues were approximately $2 billion. This compares to the $11.6 billion in revenues realized from the carriage of international passengers. The amount of international air freight flown by U.S. carriers as measured by revenue ton miles has approximately tripled since 1980. U.S. market share of the movement of freight between the U.S. and other countries has declined markedly since the mid-1970s from 42% to approximately 30%. An April 1988 Analysis of the United States International Air Cargo Market by the U.S. DOT and State Department concluded that this decline was due to countries with fast growing economies pursuing policies of aggressive development of air freight services.

In May 1989, the DOT issued a Statement of U.S. International Air Cargo Policy intended to guide U.S. aviation negotiators. The Statement called for specific treatment of cargo issues in aviation negotiations and for comparability of air cargo opportunities between U.S. and foreign carriers.

The policy statement grew out of hearings in the late 1980s by the Subcommittee on Investigations and Oversight that revealed that not enough attention and emphasis was being placed on the cargo side of international air transportation by U.S. policy-makers and negotiators. This lack of emphasis resulted in quality and cost of service problems for the shipping public and competitive disadvantages for U.S. carriers.

The following table provides a summary of U.S. carriers international freight revenues for 1989 and the relative importance of the different world regions to each carriers freight operations.

U.S. Airline International Cargo Revenues
1989
(in $ millions)

Airline	Total	Pacific	Atlantic	Latin
Fed. Exp.	$959	$370	$589	----
Northwest	358	334	24	----
United	188	188	----	----
Pan Am	164	----	115	49
TWA	93	----	93	----
Delta	87	41	39	7
American	85	7	56	21
Continental	74	51	19	4
Eastern*	12	----	----	12
USAir	1	----	----	----
Total:	$2,021	$991	$935	$93

*Eastern's Latin American route system was transferred to American Airlines on May 3, 1990.

U.S. International Airline Finances

In 1989, the U.S. airlines received $13.626 billion in revenues from providing international services, not including services to Canada (1989 data on Canada are not yet available, but 1988 U.S.

carrier revenues for Canadian services were $1.89 billion). Total international operating expenses were $13.698 billion for a net operating loss of $71.8 million in 1989. 1988 was a much better year for U.S. international operations. In that year, over $825 million was made on $11.4 billion of revenues.

1989's poor performance can be attributed to start-up costs of new services by a number of carriers, expansion of capacity in some markets, softening of traffic growth, and financial hemorrhaging by Pan Am and Eastern. Even so, this 1989 marginal loss does not reflect the international airline business picture in a uniform way. There were significant profit and loss centers within the international system for U.S. carriers.

The following table provides financial data for U.S. international airlines.

Summary of U.S. Airline International Revenues and Expenses

(Passenger and Cargo)

1989

(in $ millions)

Routes	Operating Revenues	Operating Expenses	Operating Profit/(Loss)
Atlantic	$5,937	$6,270	(333)
Pacific	5,779	5,426	353
Latin	1,910	2,001	(91)
Canada*	1,840	N/A	N/A
Total	$13,626	$13,697	(71)

*Canada data is for 1988. The $1,840 million is not included in the total.

As the table indicates, the Pacific routes were profitable, while Atlantic and Latin routes were unprofitable. This is why there is intense interest by all major U.S. carriers in expanding or breaking into the Pacific markets, particularly Japan. The Asian market is expanding rapidly, and yields are relatively high due to the restrictive pricing regimes of the bilateral agreements.

The following table depicts the relative size of U.S. international airlines' operations and the relative importance of different world regions to each carrier's operations.

U.S. Airline Revenues by World Region
(Passenger and Cargo)
1989
(in $ millions)

Airline	Total	Atlantic	Pacific	Latin
Pan Am	$2,655	$1,920	----	$735
Northwest	2,610	380	2,310	----
United	2,179	----	2,179	----
TWA	1,590	1,590	----	----
American	1,291	721	106	464
Fed. Exp.	1,084	671	414	----
Continental	1,048	236	225	588
Delta	868	462	191	216
Eastern*	257	----	----	257
USAir	44	30	----	14
Total:	$13,626	$5,937	$5,779	$1,910

*Eastern's Latin American route system was transferred to American Airlines on May 3, 1990.

Status of Relations with Major Aviation Partners

The following provides a brief description of the aviation relationship between the U.S. and its largest aviation partners.

Canada

Canada is the United States' largest aviation partner. Though it is the largest, analysts believe that there is great amount of unfulfilled demand for air travel between the two countries because the bilateral agreement is highly restrictive. Routes and services are quite limited, and all pricing decisions must meet government approval. Negotiations to expand the number of routes and liberalize the relationship have taken place for years with only small progress being made due to Canadian concerns over its small carriers' ability to compete with the large U.S. carriers in a liberal environment.

It now appears that both the Canadians and the U.S. are very much interested in initiating negotiations to liberalize the relationship. Talks are expected to begin next year. Canada is likely to bring some form of cabotage for Canadian carriers within the U.S. to the table. If cabotage were agreed to, Congress would need to pass legislation to implement an agreement.

United Kingdom

The U.S.-British aviation relationship has been a quite stormy one for years. In 1976, the U.S. and the U.K. came very close to ceasing air service between the two countries over a dispute on drawing up a new bilateral agreement. British Airways is no longer owned by the British government, but the government continues to go to great lengths to protect British Airways' position in the marketplace. The agreement is a traditional, conservative one, but in practice there is a relatively high level of fare competition and services between the two countries.

One issue that has festered for years is the landing fees charged to U.S. carriers at London/Heathrow Airport. The U.S. government believes the high fees are discriminatory against the U.S. carriers. The U.S. and the U.K. governments are now engaged in arbitration at the World Court over the issues.

Another outstanding issue is a complaint filed with the DOT by American Airlines against the British Airport Authority. American does not have the ability to provide itself ground services at Gatwick Airport and wants to do so. The U.S. government has not yet taken a position on the complaint.

Earlier this year, an agreement was reached to provide two new routes between the U.S. and Manchester. Several U.S. carriers are seeking those routes through an ongoing DOT proceeding. The British were awarded two new routes as well from secondary British points to the U.S.

Japan

Last year, the U.S and Japan reached an agreement permitting a significant expansion of service between the two countries. Under the agreement, each country will designate for its carriers three new passenger routes between the U.S. and Tokyo, three new passenger routes between the U.S. and a Japanese point other than Tokyo, a new cargo route, and 450 charter flights per year.

The U.S. has designated UPS for the cargo route, but UPS is having difficulty in securing the slots it needs at Tokyo to provide the service. Until the issue is resolved, the Japanese carrier will not be permitted to initiate its new service at Chicago. It had been scheduled to do so last week.

The DOT has a route proceeding underway to designate the carriers for the six new passenger routes. All major carriers are seeking authority. Decisions are anticipated in November.

The U.S.-Japan bilateral is a traditional restrictive agreement. The U.S. would like to see a much more competitive environment established, but the Japanese have no interest in this as they are fearful that the large U.S. carriers would further expand their market share. There is also no U.S. airline constituency for a truly competitive regime with Japan as fares in these markets are some of the highest yielding in the world.

The Japanese also want a new bilateral but for wholly different reasons than the U.S. They view the current one as a product of post-World War II occupation and as very unfair to the Japanese. The Japanese point to the fact that while only 24% of the traffic are U.S. citizens, U.S. airlines carry 55% of the traffic. The Japanese feel that the bilateral should be changed to reflect a more equitable distribution of the traffic from their standpoint meaning U.S. rights would be cutback.

Because the U.S. and Japan are philosophically polarized on aviation issues, the current bilateral will likely remain in place for the foreseeable future, and periodically, incremental expansions of services will be made.

Mexico

In 1988, the Mexican government made a fundamental change in its approach to its civil aviation relationship with the U.S. by deciding to aggressively promote and attract tourism. To accomplish this, the Mexicans are permitting a large expansion of new route authority for U.S. carriers. In some cases, multiple U.S. designations over the same route are being permitted. Prior to this policy change, Mexico took a more traditional approach of sheltering its national carriers from competitive forces. U.S. airlines are expanding their service to Mexico.

Germany

The U.S and Germany have a relatively liberal and competitive relationship. Though pricing is relatively competitive and open, the U.S. would like to make it more so.

The unification of West and East Germany resulted in Pan Am selling its rights to provide inter-German Berlin services to Lufthansa for $150 million. Prior to unification, Berlin air services had been largely regulated by the former World War II Allies with Lufthansa not being permitted to serve Berlin. Reunification destroyed the rationale for this arrangement.

France

The U.S. and France also have established a relatively liberal aviation environment operating between the two countries, however, a perennial issue between the two countries is France's desire to limit capacity increase by U.S. carriers. A recent agreement required the U.S to state what the capacity expansion plans of U.S carriers would be for the next two years. Expansion will be limited to that, but it largely reflects what U.S. carriers want to fly during that period.

This recent agreement also provided for new Chicago-Paris route authority for United beginning next summer and Dulles/Washington-Paris authority beginning in the Summer of 1992.

United very much wanted this service to commence sooner. The agreement also provided that cargo carriers would have the right to carry cargo originating in France beyond to other points on flights that originated in the U.S. (Fifth Freedom Rights).

International Aviation Issues for the 1990s

Outside of the "routine" international aviation issues, U.S. policy makers will be confronted with a number of very important developments with very significant policy implications.

European Community Integration - The European Community plans to integrate its economies beginning in 1992 by reducing barriers to flow of goods, people, and money across borders. Integration presumably will include a liberalization of civil aviation relations within Europe. A major issue for the U.S. is to what extent the liberalization will spill over to relations with non-European countries. There are concerns that European integration could result in a loss of rights for the U.S. within Europe unless the U.S. is prepared to permit cabotage to some extent within the U.S. for European carriers. There has been considerable speculation that after 1992, intra-European routes could be considered cabotage for non-European carriers. There is also uncertainty as to who the U.S. will negotiate with after integration, individual countries or representatives of the multilateral community. Among U.S. airlines, there is a sense that it is very important to obtain as many European rights as possible before 1992, given the uncertainty of the US-Europe relationship post 1992.

Foreign Ownership of U.S. Airlines - Over the past few years there has been increasing interest by foreign carriers in investing in U.S. airlines. While most of the investment so far has been relatively small so as not to exceed the U.S. control and ownership requirements, the 1989 KLM arrangement with Northwest was redrawn because of DOT concerns about foreign control of Northwest. Also SAS arrangement with Continental raised questions of control though the DOT approved that arrangement.

Most industry analysts anticipate that the airline industry will become increasingly global in its operations thereby increasing the interest in relaxation of foreign ownership restrictions not only of the U.S. but other countries as well.

Adequate Airport Capacity; Here and Abroad - Growth of civil aviation is not only outpacing the U.S. aviation infrastructure but Europe's and Asia's as well. In fact, aviation infrastructure problems are far more acute in Europe and Japan than in the U.S. As service expansions are negotiated, policy makers will have to be increasingly cognizant of access and infrastructure problems that may negate or diminish the benefits of new negotiated service rights. On the bright side, there are a number of significant new airport projects underway in Asia that will improve the capacity situation in that part of the would later this decade.

Implications of Financial Problems of Some U.S. Airlines - Two of the U.S.' international airlines, Pan Am and TWA, are in deep financial difficulty, and there is a great deal of speculation over whether they have a long term future. International route authority is a valuable asset that could be sold off by these carriers in an attempt to survive or to satisfy creditors in a bankruptcy. In fact, pending before the DOT, is a proposed sale of TWA's Chicago-London route to American. Another example of recent route transfers was the sale of Eastern's Latin American routes to American after Eastern declared bankruptcy.

Given the extensive route authority of these two carriers, the composition and market share of U.S. carriers in Europe could change very radically if large amounts of route authority were put on the block for sale. DOT policy makers would approve or disapprove of these route transfers. Their decisions would have very significant implications for the future structure of the world's airline system.

General Agreement on Trade in Services Negotiations - The ongoing negotiations over a future Trade in Services Agreement could include

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some aspects of international airline services in a General Agreement on Trade and Tariffs framework. Depending on to what degree aviation services are included in an agreement, the scope of bilateral civil aviation agreements and negotiations could be significantly lessened. The Committee held hearings last November (Committee publication 101-23) on the implications of airline services in a G.A.T.T. type arrangement. The Committee leadership is strongly opposed to including international air services in a G.A.T.T. Trade in Services Agreement, believing it would weaken the strong U.S. negotiating position in civil aviation matters and result in protracted resolution of disputes that are able to be resolved relatively quickly bilaterally.

REVIEW OF INTERNATIONAL AVIATION POLICY AND BILATERAL AGREEMENTS

THURSDAY, OCTOBER 11, 1990

U.S. House of Representatives,
Subcommittee on Aviation,
Committee on Public Works and Transportation,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:55 a.m. in room 2167, Rayburn House Office Building, Hon. James L. Oberstar (chairman of the subcommittee) presiding.

Mr. Oberstar. The Subcommittee on Aviation will please come to order.

This morning we both begin and resume hearings to review international aviation policy and our bilateral agreements. It is perhaps an unusual hearing from the standpoint of the tradition of this subcommittee of having the same day a wide variety of witnesses. Today we will hear only from the Department of Transportation and its very gifted, talented, and highly experienced Assistant Secretary for Policy and International Affairs Jeff Shane.

At a later date, we will take testimony from other witnesses; and we will proceed in that fashion. I assure all of those who have a very burning interest in this issue that the usual widerange of interests will be presented. We intended to hold these hearings in late July or right after Labor Day. However, our work on the reauthorization bill for aviation programs consumed more time than we had anticipated. A number of other matters, including aviation security, intervened; and so we have had to truncate this hearing. But both Mr. Clinger and I felt it was something we must do before the close of this session, assuming it does close within the next 30 days or at least before election and that we don't have a lame-duck session. So I want to emphasize that this is the beginning of a much needed review of aviation trade policy.

Travel overseas aboard U.S. aircraft by our fellow citizens is a very powerful sector of the national economy. Both foreign travel and cargo shipments are increasingly the mainstay of the way in which trade is conducted among Nations. The most highly prized and highly valuable cargo moves by air, and people seeking travel for leisure pleasure, and especially for business, go by air rather than surface vessel. Congress needs to be sure that U.S. policies are working as effectively as possible to promote U.S. interests, including the U.S. travelling and shipping public, our carriers, and the communities those carriers serve.

Last year, foreign travel to the U.S. exceeded for the first time in balance of payments U.S. travel overseas. Travel to the United States generated $1.8 billion more than U.S. travellers spent abroad. That was the first time since the U.S. Travel and Tourism Administration has been keeping records that we have achieved a surplus balance of payments. I feel that the turnabout is due to a number of factors. One, that the U.S. TTA is being much more effective in its overseas promotion of travel to the United States. Secondly, the longstanding efforts at improving U.S. aviation trade with our trading partners has borne fruit.

I begin these hearings with a sense that U.S. policy, U.S. negotiating strategy, and negotiating tactics, are more effective and overall in better shape today than they were five or six years ago. I think also a factor is that we maintained a continuity in the persona of those negotiations. Mr. Shane has been an experienced, seasoned hand in negotiating international agreements from his earlier days with the Department of Transportation, then with the Department of State, now back to the Department of Transportation. I recall, when Mr. Clinger and I first began this inquiry into international aviation trade policy in the Investigations and Oversight Subcommittee, learning with amazement that the chief Japanese negotiator then was the same person who negotiated the 1952 bilaterals between Japan and the United States. He continued to remain in that position, outliving and outpacing all the successions of persons who occupied counterpart positions in the U.S. Government over three decades. Well, that puts our negotiators in a rather difficult position, to say the least. There is a lot of catch-up to do and the institutional memory is with the Japanese negotiator rather than with the U.S. negotiator. Well, I now feel that we have both institutional memory and seasoned experience and effectiveness in the person of Mr. Shane, who has his sense of where the bones are buried and where the commitments were made and where the concessions were made and what we ought to get in exchange.

Further, the framework within which aviation trade is conducted is unique—the bilaterals. These provide a framework within which we have the strongest possible trading position in any economic sector in which we conduct foreign trade, for we are in a position to exchange rights for rights and values for values. You can't do that in automotive trade, or in computers or electronics or VCRs or color TVs, and that is why we have lost our market and lost our shirt.

The third reason for this hearing is that I have a sense that aviation trade may be on the cusp of a major turning point in the evolution of this dynamic trade sector. We are perhaps at a point where we may be moving beyond the concept of bilateral to a new trade regime. Now is the time to assess the effectiveness of the bilateral, what changing it may mean for the future, what it may mean to question some fundamental concepts within that bilateral arrangement, some of which—in fact, most of which are going to be discussed in Mr. Shane's testimony; and the strength of U.S. carriers at this point. I think it is one thing to make major changes in aviation trade policy when U.S. carriers are strong and effective and in a good position to compete, but a very different matter should they not be so positioned. We need to assess the condition of the U.S. air carrier fleet as they meet our foreign competition.

So we need to focus on whether necessary steps are being taken to adapt U.S. policy in aviation trade to a changing international political and economic regime, to the dramatic movements not only in the European Common Market that are underway with a deadline of 1992 and the slow evolution now, but rapid evolution that will take place after that, to the stirring events of Eastern Europe, the mounting challenge from the Pacific Rim, and to assure ourselves that our policymakers are taking time to think both short-term tactics and strategy and long-term policy to prepare for these sea changes that are occurring in international aviation trade.

The Chair recognizes the gentleman from Pennsylvania, Mr. Clinger.

Mr. **Clinger**. Thank you very much, Mr. Chairman.

As you have indicated, the future viability and competitiveness of today's large domestic carriers is going to heavily depend on their ability to compete effectively in international markets, which is the point of our initial hearing today on this question of international aviation. As a result of mergers and fleet expansion, U.S. carriers have fairly much saturated the domestic market and future profitability of these companies to a large degree rests on developing and sustaining international markets. Certainly if we look at what has happened with such airlines as American, Delta, and United in the last several years, carriers that a decade ago were almost exclusively domestic in their routes, and in today's market a carrier may well jeopardize its future growth and profitability if it fails to pursue international service.

So as carriers seek to expand, the importance of maintaining an aggressive but fair system grows. And, as you have indicated, that may mean that we are moving away from the bilateral to some new system. I think we ought to explore that. Coincidentally, at the same time U.S. flag carriers are seeking to expand overseas, so too have foreign carriers sought to expand their markets abroad and into the United States.

I think that our system of bilateral agreements have to date served us well in maintaining relative parity with foreign carriers. But I believe that as competitive forces gain momentum and as multinational business alliances grow, international boundaries will become blurred and we should be prepared to rethink our system of bilaterals to ensure that the American consumer and U.S. flag carriers continue to be well served and remain competitive.

We have, Mr. Chairman, as you know, a number of controversial issues in this area that we will be exploring in this hearing with Mr. Shane and in future hearings. Certainly the doing business issues are a major concern. Where we have had experiences under bilateral agreements where a foreign nation will grant a route and then pose many difficult impediments that make that route not really worthwhile, most recently with the UPS situation and Japan. I think the question of cabotage is certainly a very controversial issue, one that is going to be raised I am sure in connection with the recent agreement with Canada, and there will be other areas where that is going to emerge. Also, the question of foreign ownership of U.S. airlines I think is an issue that we're going to be considering and exploring. So there is no lack of controversial and challenging issues to be considered here.

I certainly am glad that we are holding this hearing and look forward to hearing from Mr. Shane, who has been a most valuable witness before this committee on so many occasions, and our witnesses in the future.

Thank you.

[The prepared statements of Mr. Clinger and the Hon. Costello follow:]

STATEMENT OF HON. WILLIAM F. CLINGER, JR.

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As a result of mergers and fleet expansion, U.S. carriers have fairly much saturated the domestic market, and future profitability of these companies to a large degree rests on developing and sustaining international markets. Witness the number of international points added by American, Delta, and United in the last several years, carriers that a decade ago were almost exclusively domestic. Indeed, in today's market a carrier may well jeopardize its future growth and profitability if it fails to pursue international service.

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Our system of bilateral agreements have to date served us well in maintaining relative parity with foreign carriers. But I believe that as competitive forces gain momentum, and as multi-national business alliances grow, international boundaries will become blurred and we should be prepared to rethink our system of bilaterals to insure that the American consumer and U.S. flag carriers continue to be well served and remain competitive.

I want to thank our witness, Mr. Shane, for taking time from his busy schedule to appear before us today. I look forward to hearing his statement.

Thank you, Mr. Chairman.

STATEMENT OF REPRESENTATIVE JERRY COSTELLO

Mr. Chairman, I am pleased to be here to address upcoming issues in international aviation policy. As international air travel increases and becomes more interdependent, policymakers face new challenges in negotiating with our international partners.

Some of the issues which I hope to hear our Department of Transportation witnesses address today include the effect of integration of the European Community on U.S. market privileges in Europe; the development of airport capacity both within the United States and in other countries; and the exclusion of air services from General Agreement on Tariffs and Trade talks. I thank them for coming and I thank you, Mr. Chairman, for convening this hearing.

Mr. **OBERSTAR**. Thank you.

The gentleman from Tennessee, Mr. Duncan.

Mr. **DUNCAN**. I have no statement, Mr. Chairman.

Mr. **OBERSTAR**. Thank you.

We are very pleased to have this morning the very able, diligent, hard working, and seasoned international trade expert in aviation matters, Assistant Secretary Jeffrey N. Shane.

Jeff, it is a pleasure to have you with us again. Please proceed.

TESTIMONY OF HON. JEFFREY N. SHANE, ASSISTANT SECRETARY FOR POLICY AND INTERNATIONAL AFFAIRS, U.S. DEPARTMENT OF TRANSPORTATION

Mr. SHANE. Thank you very much, Mr. Chairman. It is a delight to be back again. And thank you very much for those kind words.

I was thinking as you spoke that our negotiating policy has profited from some additional continuity over the years on the Executive Branch side, but it has also profited in no small way from the fact that there has been enormous continuity in the congressional oversight of the negotiating process; and I am speaking of you and Congressman Clinger and your work both in Investigations and Oversight and now on the Aviation Subcommittee. We have had a long dialogue over many years and I think that nobody could possibly say that the negotiating policy of the United States has not profited enormously from your attention to it and from that continuing dialogue.

Before I get into the substance of what I want to say, Mr. Chairman, I come this morning with what I think is a pretty good story to tell. I don't want to tell that story, however, without at least acknowledging the fact that we find ourselves in a uniquely difficult situation right now in the U.S., indeed, in the world aviation industry. The dramatic increase in fuel prices coming on top of a softening demand that was attributable to economic conditions generally has meant that we will probably have the worst quarter, possibly, in aviation history at the end of this year.

In talking about some of the successes we have enjoyed on the international aviation front, I just don't want to appear to be a mindless pollyanna. We are losing a lot of sleep over the current economics of the airline industry and, of course, we are hoping that it is a short term, rapid turn-around situation; we pray that will be the nature of the problem. But the fact is that we are nevertheless focused on it. We will be talking today about the longer-term, and I think that is absolutely appropriate. I just didn't want to appear to be oblivious to what is going on in the airline industry as we speak.

Mr. OBERSTAR. I think that is an appropriate caveat at the outset and I appreciate your raising it. The jump in fuel prices, it is estimated on an annualized basis, will cost the U.S. air carrier industry an additional $6.5 billion this year just in increased fuel prices. So that erodes profitability and has serious impacts, as you rightly noted.

Mr. SHANE. Absolutely.

Mr. Chairman, I have a long prepared statement which I would like to submit for the record and, with your permission, I would like to deliver this morning a somewhat shorter statement as a summary of that prepared statement.

Mr. OBERSTAR. You may proceed as you wish. I have read the entire prepared statement; it was an excellent one. I think you would do well to highlight the key points in it as they are many and they are important, so take the time that you need to elaborate.

Mr. SHANE. Thank you, sir.

Under Secretary Skinner's leadership, we have been actively pursuing international aviation policies designed to expand the service options and economic benefits both to the travelling public and communities that receive service, on the one hand, and, of course, for the U.S. aviation industry that provides it, on the other.

We are achieving very positive results from these efforts, and I am pleased to report that U.S. cities and U.S. airlines are doing very well. In 1989, there were 115 more international non-stop combination services operated to U.S. cities than were operated in 1984. Over that same period, ten U.S. cities received direct international air service for the very first time.

Our airline industry has benefitted substantially from the growth and expansion of the international aviation market. In 1989, U.S. airlines carried more international passengers and more international freight than the airlines of any other nation.

Charts reflecting these developments are attached to my prepared testimony, Mr. Chairman, and I would ask that those charts be made part of the record of this proceeding as well.

Mr. OBERSTAR. Without objection, so ordered.

Mr. SHANE. Although we are pleased with the growth of international air service in recent years, we believe that greater progress can be made. A major problem is that the current system of bilateral air agreements, to which you have referred, still relies to too great an extent on government regulation of air services. In our view, this inhibits the achievement of the potential economic benefits that both the United States and foreign countries would derive from a more competitive, more market-driven air transportation regime. We have recognized this problem and have taken initiatives to address it.

To further expand international aviation opportunities, DOT, under Secretary Skinner, has pursued a progressive aviation negotiation policy by proposing "open skies" aviation agreements with several of our largest aviation partners. As expected, the idea of open skies regimes is appealing to some countries, but most remain reluctant to move into an aviation environment that places full reliance on competitive market forces.

What I would like to do now is review some of the things we have been doing to advance that quest for a freer, more competitive international air transportation system.

Looking first at some of our bilateral situations, at the moment some of our most exciting prospects we think are with Canada, our largest aviation partner. Last week, Secretary Skinner and his counterpart in Canada, Transport Minister Doug Lewis, announced that the two countries would begin negotiations to create an open aviation market that would dramatically expand air services between our two countries. They hope to achieve an open regime that would permit all types of air service between any cities in the two countries by all U.S. and Canadian airlines.

In 1989, we began negotiations with Germany—our fifth largest international aviation partner—on expanding opportunities for both countries in the context of one of those open skies agreements that I referred to. A primary goal of that negotiation would be to achieve a much more liberal pricing environment than currently exists.

Also in 1989, we concluded a new agreement with Japan, our third largest aviation market, that represents the most dramatic expansion of service across the Pacific since the original U.S.-Japan bilateral agreement was signed in 1952.

Although we have made substantial progress in expanding aviation opportunities to and from Japan, congestion at Japanese airports, particularly at Tokyo's Narita airport, continues to be a major obstacle to opening up the Japanese market. A current problem, that we heard about this morning from Congressman Clinger, has arisen from the Department's recent award of authority to UPS to operate an all-cargo service to Tokyo under the terms of that 1989 Memorandum of Understanding. UPS has been unable to obtain certain evening slots at Narita that it has requested. We believe that UPS is correct in its assessment that it cannot compete effectively without those evening departures and, therefore, until that issue is resolved satisfactorily, we will withhold the issuance of authority to JAL and NCA, the two Japanese carriers that received all-cargo operating authority to Chicago under that same 1989 MOU.

We have recently increased air service with Mexico, our fourth largest international aviation partner, as a result of a much more expansive bilateral air transportation agreement that we signed in 1988.

We have also made some incremental progress in expanding the U.S.-U.K. air transportation market, which is our second largest international passenger market. In an agreement reached earlier this year, we gained three additional opportunities for U.S. airlines to serve U.K. cities other than London. We have some serious "doing business" problems with the British—one is the level of user charges which are imposed on U.S. airlines at London's Heathrow Airport. That problem is in formal international arbitration at the moment. Another problem involves American Airlines' inability to handle the check-in of its own passengers with its own personnel at London's Gatwick Airport.

Looking beyond the bilateral negotiating front, in January of this year Secretary Skinner announced our New Cities Program. This program grants foreign airlines authority to operate what we call extra-bilateral services to U.S. cities under certain well-defined circumstances. Those circumstances have been carefully developed and defined to strike a sound balance between the need for improved international service and the need to maintain a strong and competitive U.S. carrier industry. Under that Cities Program, we have granted KLM authority between Amsterdam and BWI; we have granted Ladeco, a Chilean carrier, operating authority between Santiago and Washington; Lufthansa has been authorized to fly between Frankfurt and Charlotte; and Swissair between Zurich and Philadelphia.

To further advance our policy objectives, we are also considering alternatives to the bilateral negotiating process. As you are aware, the European Community plans to form a single aviation market. That presents both opportunities and problems, both in the context of the Community's developing external aviation policy as well as in its internal aviation legislation.

There is an apparent consensus within the EC that it will eventually establish a common external policy and a coordinated negotiating approach to outside countries, like the United States. The precise shape and timing of the external policy, however, are far from settled and the Commission's proposal for unified EC aviation negotiations is at this time still highly controversial within the Community itself.

Multilateral negotiations with the EC could offer, we think, a great opportunity to liberalize aviation services, simply because the Community could bring a lot more to the negotiating table than any one of its twelve members States can, each of whose home markets is so much smaller than our own. We hope that the EC will resolve the economic and political issues involved in establishing a common negotiating front in a way that will promote broader exchanges of market opportunities with us and with other third countries.

Now I would like to address a number of the other important issues concerning international aviation policy.

Let me turn first to airline citizenship issues. The 1980s were characterized by an accelerating trend toward a globalization of the world's airline industry. Airlines worldwide have made numerous linkages to put themselves into new and better competitive positions for the future. These linkages include cross-border investments, marketing agreements, and the development of multi-carrier ownership of computer reservations systems, just to name a few.

The Department of Transportation wants to do everything possible to ensure that the U.S. airline industry remains strong and competitive in this evolving global environment, while at the same time maintaining strict adherence to the statutory requirements that U.S. carriers meet certain citizenship standards. These standards include, in particular, requirements that U.S. air carriers be citizens of the United States, as defined by the Federal Aviation Act, and that U.S. air carriers actually be controlled by U.S. citizens. The Department's decisions in recent cases involving foreign investment in U.S. air carriers reflect these considerations.

Another area affecting international aviation that the Department is actively involved in is ensuring that foreign governments and foreign carriers allow U.S. carriers to exercise fully their aviation agreement rights and that carriers can compete on a fair and level playing field.

Congress has enacted laws designed to address unfair competitive practices and DOT has made effective use of those laws whenever necessary.

Constraints on the availability of facilities and operating rights limit the ability of carriers to respond to market conditions and to compete freely. One area of particular concern in that regard is the availability of landing slots at major international airports.

Recognizing the need for carriers to have access to airports at times that will enable them to compete effectively with one another, our policy is to try to make available to carriers slots at times they want at our slot-controlled airports. We have had some problems with our carriers obtaining landing slots at certain foreign airports. I have already referred to the situation at Tokyo. Up to now, we have been successful in resolving those problems through discussions with the foreign governments involved. But we do have the authority to take remedial action where necessary, and we are certainly prepared to do so to ensure that our carriers obtain fair treatment in all of the markets in which they operate.

Another area of international air transportation that we are particularly focused on at the moment is aviation security. As you know, Mr. Chairman, we have been carefully considering the recommendations of the President's Commission on Aviation Security and Terrorism, of which of course you were a member, since the report was issued in May. We are in the process of implementing now many of the recommendations contained in the report, and I know that you are familiar with our efforts in that regard.

We are particularly pleased with the performance of our Civil Aviation Security Liaison Officers in Europe. We have a few more inspectors and liaison officers to place in Europe and also the Middle East, and we have begun the process of placing people in Latin America and Asia as well. Along with these placements will come improved cooperation and we know better communication both with our air carriers and with the foreign governments involved.

Let me assure you that Secretary Skinner and the Federal Aviation Administrator, Admiral Busey, place the highest possible priority on improving our international aviation security and we will all be actively supporting those efforts by working closely with Vice Admiral Robbins and his staff in the Department of Transportation's new Office of Intelligence and Security.

I might just add as an aside, Mr. Chairman, that one of the truly remarkable aspects of this entire episode has been the contribution made by the families of the victims of Pan Am 103. In my experience, I don't think I have seen any precedent for the active involvement of these families and the contribution that they have made to the thinking of both your branch and our branch of Government and to the shoring up of international aviation security around the world. The quality of the security that you see in place today, which is simply head and shoulders above what it was a year ago, is a lasting legacy to those who died on Pan Am 103 and to the enormous amount of effort that the families have put in. They deserve enormous credit for the work that they have done in ensuring that our Government takes this problem as seriously as we are now doing.

As a final issue, and related directly of course to aviation security, I would like to review the status of the proposed Montreal Protocols that would amend the Warsaw Convention and, specifically, the passenger liability provisions of the Warsaw Convention. Of course, the President's Commission on Aviation Security and Terrorism made a very specific and a very strong recommendation that the Senate ratify the Montreal Protocols.

The Convention currently limits air carrier liability for passengers killed or injured in international air accidents to $75,000 per passenger. Just to give you an idea of what an anachronism that is, the average recovery for passenger deaths in air accidents that are not covered by the Warsaw Convention today exceeds $800,000 per passenger.

The Montreal Protocols currently pending before the Senate, coupled with a supplemental Compensation Plan formulated by the airline industry and approved by the Department of Transportation, would provide for unlimited per passenger recovery in international aviation accidents.

In June, the Senate Foreign Relations Committee voted to recommend that the Senate give its advice and consent to the ratification of the Protocols with the Supplemental Compensation Plan, and we hope that the Senate will take up the Protocols very soon. Mr. Chairman, I just can't overstate the importance of ratifying the Montreal Protocols. We are working very hard to ensure that, indeed, the Senate does take them up before the end of this session.

I'll stop there. I hope this testimony has been helpful in apprising the subcommittee of the extensive work that we are doing right now on international aviation issues. I look forward very much to answering any questions that you or other members may have.

Mr. **OBERSTAR**. Thank you very much, Mr. Shane. We really appreciate your comprehensive overview of the state of international aviation trade, the very extensive work underway over the past year and a half, almost year and three-quarters, under your leadership. Again, let me restate that I felt awfully good, as I know Bill Clinger did, that you were brought into the Department to shepherd U.S. aviation trade negotiations. You bring a steady hand and a seasoned hand and a lot of experience to dealing with the international participants, if you will, on the scene.

There have been some very significant developments. We really do now have a cargo policy, we do have a consistent pattern of trade negotiations on passenger carriage, and we have been consistent in applying our principles. Particularly, I want to compliment you on standing firm on Japan with the issuance of authority to Japan Air Lines and Nippon Cargo Airlines. The start-up of NCA trade with the United States was one of the first issues. They wanted so desperately to get into the United States and they wanted so desperately to be in the Chicago market, and yet they weren't giving our carriers in Japan the same rights that they wanted in the United States. So instead of starting up that trade on April 1, they waited a month after a rather vigorous inquiry at one of our hearings. Frank Willis at the time, as I recall, was the State Department negotiator. It was amazing how the Japanese came around and yielded on a number of points and NCA began its trade. Now they have got the access to Chicago and they are upholding rights again. We went through this with United Air Lines when they acquired Pan Am's Pacific division. Now it is UPS that has service and the Japanese aren't allowing them to exercise that service. Well, if that right does not carry with it economic value, then it is of no meaning. So you are doing the absolutely right thing in withholding authority to provide service to Chicago until they see the light and come around and deal with us.

I appreciate your observations on security. I think that is very important that the Department has moved as incisively as it has. You stated the case I think very well that the, indeed, the families of the victims can never regain their loved ones but can only honor their memory by seeing that travel for others in the future is made more secure. They have bent every effort towards this end and the result has been the President's Commission on Aviation Security and Terrorism, its report, the Department's response, and legislation that soon will be through conference and to the President for signature incorporating many of the actions already undertaken by the Department and enacting into law many other of the recommendations of the Commission.

You have taken some positive steps with respect to the Cities Program. You are looking far ahead—maybe a year or two years—in the fast changing pace of international aviation trade to developments in Europe, and I think wisely so, anticipating the chain of events that may unfold as Europe becomes more completely a single market than it is today with lots of questions that the Europeans haven't yet resolved internally about how aviation trade will be conducted in Europe. I will come in more detail to that later.

I feel very good about a number of those matters. Oh, yes, and the action on complaints against discriminatory practices against U.S. carriers on Computer Reservation on CRS Systems, that is cited in your testimony. You have acted more decisively within a shorter time frame. A complaint process is of no value again if it isn't acted upon. It takes years to resolve these matters. So congratulations.

There is one area where I must say I disagree with what the Department has done and that is in foreign ownership, foreign investment in U.S. carriers. In a number of respects, the recent SAS investment in Continental was modified by the Department for the better. But I still feel very strongly that the Department should have required the SAS voting interest to be pared down to 5 percent and the balance put in a non-voting stock. It is rather clear given who is on that board that if everyone else has less than 5 percent and SAS has 18 percent, even though they are well below the 25 percent threshold that constitutes control, we come to a different conclusion on the independence of that board of directors. There are some strong personalities, no question—I know a couple of them and they are, indeed, strong personalities—but in the final analysis there is an old saying about money talks and something else walks. In this case, the money is going to talk and we will see whether in the long-run the Department's judgment was right. I urge, now that the decision is made—and I have written a letter of concern about it—that the Department follow it very closely, as was indicated will be done.

The reporting requirements are very strong, very important, but if they are not exercised, then you are dealing with a very shrewd, powerful, effective international aviation trade personality in [SAS chairman] Carlzon, whose interests extend to a number of other carriers. He is no babe in the woods, he is no innocent little starry-eyed investor; he is in there to make money. He didn't buy a ticket to the game, he bought a seat on the bench next to the coach and he intends to more than whisper in his ear. So you have taken on a responsibility that I expect and urge to be carried out.

And then the matter of Northwest Airlines. I think the Department did the absolutely right thing there. Again, I am dismayed that the Office of Management and Budget came back, when we passed our Leveraged Buy-Out legislation last year, and sidetracked that bill over in the Senate. All we wanted to do was codify what I thought were some very wise, responsible, and visionary decisions by the Secretary. I have a question in that regard. Did Northwest Airlines meet the September 30 deadline the Department set for adjusting KLM's holdings, buying that down to the level agreed upon? And secondly, have you examined the $500,000 loan to Northwest? Questions have been raised about its propriety and I think we ought to just lay those out on the table here and see what the Department has done about that.

Mr. **Shane**. First, Wings Holdings came to us well in advance of the September 29th deadline for that divestiture and indicated to us that although they had certainly undertaken steps to comply with divestiture, market conditions were such that undertaking that divestiture and keeping with that deadline would, in fact, be penalizing a number of the parties to the transaction. The Secretary felt, upon looking at that representation, that it was a reasonable case to make; therefore, just prior to the deadline, the Department of Transportation gave Wings an additional year within which to comply with that divestiture requirement.

As to the $500,000 loan supposedly made by Airbus in connection with the recent aircraft acquisition by Northwest, we have looked into that loan; in fact, Northwest has been very open with us in terms of their willingness to talk about it.

Mr. **Oberstar**. That's right. Thus far they have been very open about it, not concealed anything.

Mr. **Shane**. That's right. Indeed, I think they are proud of the terms that govern that loan. Thus far, it is not the disposition of the Department to take any action with respect to that. I think we want to keep our eye on financing packages of that kind. Obviously, it gets tied up in the whole question of concessionary financing and whether or not our airframe manufacturers are trading on a level playing field. But as best we understand the situation, a loan of that kind is not unheard of in the context of the kind of market that currently exists for aircraft and the kind of competition that these airframe manufacturers are waging with each other.

Mr. **Oberstar**. The concern, and you have focused on it, the concern has been raised in a number of quarters and one of them is that very matter of fairness in competition when a major manufacturer of aircraft can influence, or appear to be influencing, the market conditions. I am pleased that the Department is watching this matter carefully and also pleased that Northwest has been quite open about it. I think that's a matter that needs continued review.

Mr. **Shane**. I agree.

Mr. **Oberstar**. I will have some more detailed questions about the U.S.-Canada negotiations. There are a number of sub-issues with respect to the U.S.-Canada talks that will take place I gather early next year. In Canada, from my reading of Canadian press and other news publications, this is a very big issue. It has labor implications, it has economic implications; yet, it has raised concerns within the context of the U.S.-Canada Free Trade Agreement. What we say, what we do in this country may make the back pages, if any page, of U.S. papers; it will surely be front page news as far as Canada is concerned. So I know we have to proceed very carefully. But I do think that what the Department has undertaken with Canada can prove to be a laboratory for the future of U.S. aviation trade. That proceeding step-by-step thoughtfully and carefully is a very important initiative and I would like to explore with you some of the aspects of that negotiation and potential. I'll come back to that later.

I will now yield to my colleague, Mr. Clinger.

Mr. CLINGER. Thank you, Mr. Chairman.

Thank you, Mr. Shane, for your comprehensive and concise review of the international scene as it relates to aviation. I want to talk to you just briefly about the prospects for our relations or arrangements with the European Community after 1992. I serve as a member of the delegation that meets with a delegation of the European Parliament on a regular basis and this has been an area that I have been quite interested in for some time and have been trying to follow the Community as they wrestle with the directive both for internal operations and also external. Can you give me a sense of where they stand at the moment and how close they may be to finalizing their directive?

Mr. SHANE. Yes. Well, I am not sure how accurate my report is likely to be. I have had the impression somehow that a lot of the front page stories in Europe about the imminent liberalization and integration of the EC market have somehow drifted off the front pages to that back of the paper that the Chairman referred to. I suspect that is because the Community member states are now in the very, very hard process of actually trying to define the pace and shape of that integrated market at long last. My guess is that it is a far more difficult undertaking than perhaps even the members themselves anticipated, and that it may very well take longer than the beginning of 1993, which was when the single market was anticipated to come into force.

Until such time as they have completed that process, however long it takes, I am afraid that it will be very difficult for us to get a lot of attention from the European Community or the European Commission. We have an on-going series of informal discussions with the European Commission, including Commissioner Van Miert, who is Commissioner for Transport, and Sir Leon Brittan, Commissioner for Competition, and we have been talking about the implications of a single transport market within the European Community on a regular basis trying to anticipate opportunities, as I mentioned, and certainly bringing to their attention any problems that we see emerging from the regulations as they are formulated. Those have been profitable conversations. They understand the eagerness of the United States to begin to talk meaningfully about what the implications will be of that integrated European Market for the transatlantic market. But they also remind us on a regular basis that they simply do not have authority yet from the member states to engage us in anything like a negotiation about that. We can continue to consult about it, we continue to think great thoughts about what the future may hold, but thus far I think those of us who aspire to sit down at the negotiating table and start really working out what kinds of new opportunities might emerge from that larger market over there have been frustrated and will continue to be frustrated for a while.

Mr. CLINGER. Basically, at the moment at least, the Community cannot speak with one voice or is not in a position to negotiate with us with one voice.

Mr. SHANE. They have arranged, apparently, to speak with one voice to non-Community European countries, the so-called EFTA States.

Mr. CLINGER. Right.

Mr. SHANE. I imagine that they are learning a lot about the process of speaking to third countries through the EFTA negotiations that are ongoing now. But we are going to have to wait, I am afraid, until that process has worked its way through before they are likely to turn in our direction and talk to us.

Mr. CLINGER. You have indicated in your statement that you think the prospect of Europe 1992 poses tremendous opportunities for opening up a liberalization of aviation traffic but also has some risks to it. I am wondering what kind of assurances or what sort of a feel do you have at the moment for whether we are going to see perhaps a regression. You know, if we have a unified Europe, are we going to lose some of our Fifth Freedom rights? Is there a possibility that they will then speak as though this is only one entity and, therefore, we are going to reduce what opportunities we have in Europe?

Mr. SHANE. Well, the Fifth Freedom rights that we enjoy in Europe right now are a function of existing bilateral agreements. I don't think anybody is prepared to start withdrawing unilaterally rights that the United States has bought and paid for in the context of bilateral negotiations. Certainly, any effort to do that would trigger a reciprocal withdrawal by the United States of comparable rights, and that would be a negative. I think that the Europeans understand that would be a retrograde way to proceed as they are pulling their own market together and liberalizing it. I think what they will be interested in doing is sitting down with us and trying to figure our what kinds of opportunities the United States might be willing to exchange for even broader opportunities within Europe, at least that is certainly my hope. It would be extremely unfortunate if the liberalization of Europe translated into a contraction of the opportunities across the transatlantic market.

I can't speak very knowledgeably about the positions that individual EC member states are likely to take. I can speak with some experience about the positions that I have heard articulated informally from the European Commission. I think it is fair to say that within the Commission there is a strong feeling very similar to our own that the integration of the European Community ought to translate into a larger transatlantic market; indeed, perhaps in the longer term, even an integrated transatlantic market, although that would be a radical departure from anything that we see today. Where the balance will be struck within Europe I think is something we just have to wait and see. Everything we do is obviously aimed at encouraging the most liberal thinking within Europe in the hope that we'll see net opportunities there and not any net contraction.

Mr. CLINGER. As a somewhat ancillary area, I would anticipate one of the problems they are going to have is that as they deregulate they will find an increase in demand throughout the area. They don't really have the infrastructure at this point to handle what could be a rather dramatic increase in demand. Are they addressing that, in your view? Are they looking at the need to have an integrated Air Traffic Control System and more capacity at their airports? They may be overwhelmed, it seems to me, come 1992 or 1993.

Mr. SHANE. They are all very much aware of the limitations currently impeding traffic growth and the exploitation of the kinds of opportunities they seek to establish through integration. They are focused on it. Frankly, what the wherewithal is to expand infrastructure within Europe right now I just don't know. I think part of the problem may be relieved to some extent by an emphasis on markets which have been secondary up to now. The first real liberalization within Europe in the first phase of the liberalization of the aviation market was in city markets involving so-called secondary or regional airports. It is likely that better service to those regional airports, creating new hubs, if you will—perhaps something akin to the phenomenon we saw take place in the United States—will help to diminish some of the demand for scarce take-off and landing slots at airports like Frankfurt and Munich and Heathrow and places that really are saturated right now. We can only hope that will happen. But I am afraid that even if that does provide some relief, it won't be very long-lasting relief and that pretty soon we are going to find ourselves bumping up against the limits again.

It is a serious problem for us even now in the bilateral dealings we have with those countries. I refer in my testimony to the importance of being very focused on our own policies for granting access to airports, particularly high-density airports that are slot-constrained. Up to now, we have been very forthcoming, even to the point of pulling slots away from domestic operators, to ensure that foreign carriers get what they paid for in bilateral agreements with the United States. To the extent that it is no longer necessarily the case that U.S. carriers are going to get the slots that they need at foreign airports, obviously we need to be very focused on the kinds of rules that we employ here for the benefit of foreign carriers. We have a reciprocity provision in our own slot rule; thus far we have never used it. We aren't dealing with the slots that JAL and NCA obtained at Chicago; we have simply withheld the basic operating authority. But it may very well be that in the longer term, as slots become a problem abroad, we are going to have to focus more clearly on the way in which we distribute slots to foreign carriers here, just to make sure that nobody is ignoring the importance of solving this problem wherever it appears.

Mr. CLINGER. It just seems to me that if we have capacity as an inhibition to growth, we are going to suffer. At least that would be my guess, is that they would tend to favor their own carriers over us. I guess we are going to have another round, aren't we?

Mr. SHANE. Yes.

Mr. **Clinger**. I think my time has expired.

Mr. **Oberstar**. The Chair would recognize the gentleman from Oklahoma, Mr. Inhofe.

Mr. **Inhofe**. Thank you, Mr. Chairman.

Mr. Shane, it appeared to me when we made a limited inspection of some of the airports in Europe that there are obstacles there in terms of cooperation. Maybe I sense this more than others did and I would single out France. If it hadn't been for our Chairman's fluency in French, I think those obstacles would have been more impervious.

Let me just ask you if you feel that you are making any progress in cooperation? I will single out two areas. One was in the TNA, I know you briefly talked about this, but I got the feeling that, no, we have our own technology; well, when is it going to be on-line? Well, it is going to be two years or something. And there was a lack of interest in using our technology that I believe was advanced over theirs. They didn't concur in that. But to get something online that is uniform throughout not just Europe and the United States but throughout the world system, are you seeing any progress in getting more cooperation?

The other area I would single out would be in air traffic control. Yesterday, when we opened this technological fair over in the Cannon Building and Secretary Skinner was operating the controller computer. I was thinking at that time that the holding patterns that exist now over in Europe are interminable. They don't seem to be making a lot of progress, that I can see anyway, and they don't seem to be interested in cooperating with us or at least coming to our technology that we are willing to share with them.

How do you see those two areas specifically, and then in general just the cooperation or lack of cooperation, is there any progress being made?

Mr. **Shane**. It has been a hard pull, Congressman. I think we are beginning to see some genuine improvement in the level of cooperation. Let me just talk about aviation security.

To take France as an example, when we initially prescribed our so-called extraordinary measures in the aftermath of the Pan Am 103 event, we were, in effect, requiring U.S. airlines to break French law as it then existed. French domestic law requires that all security operations on French soil and at French airports be conducted by police, by public authorities. As you know, our rules require airlines to do it themselves and, therefore, they have private sector personnel conducting searches. Even in the beginning, my feeling was that the French were working very hard to try to figure a way to bridge the gap. In other words, they understood that we have a special way of doing things, that we had applied those rules in the first instance only to U.S. air carriers, and they worked very hard to wink, if you will, at their own law. They have since amended their law so that we are no longer even in technical violation of French law. But that was an expression of their willingness to recognize the importance of the security issue and to work with the United States in accommodating the requirements which the FAA had imposed on U.S. airlines.

There is, no doubt, a little technological competition between the United States and other countries, particularly France perhaps, in the explosives detection area. Our attitude toward that competition is that it is probably healthy. I am not sure that the French are coming on line with anything very soon that will be superior to thermal neutron analysis, and I believe the French understand that. We have said to them, if they do have a better machine, that we would be delighted to embrace it; in fact, we would encourage American carriers to buy it.

Mr. INHOFE. Okay. What was their response when you made that statement?

Mr. SHANE. I'm sorry. We know that they are interested in producing their own technology and——

Mr. INHOFE. No, no. When you told them that if they had a better machine that we want to look at it and maybe we would use yours. What was their reaction to that offer?

Mr. SHANE. Well, the fact is that they aren't in a position to produce a machine of that kind yet. I think they were encouraged to hear that we are not simply trying to capitalize on the security problem to sell American technology around the world; we are looking for the best technology we can find. Unfortunately, they weren't able to produce the prototypes that we hoped that we would see. I don't know if I am responding exactly to your question, Congressman Inhofe.

Mr. INHOFE. Yes. I was just wondering because when we were over there—and the Chairman may not have gotten the same interpretation I did from their remarks—I understood them to say, no, we are really not that interested in your technology because we have a better one. We pressed them, you know, as to when would it be on-line, when will you be able to show us what you have, and essentially saying the same thing that you just said that if you have got a better deal, let's look at it, we are not all that impressed with ours but it is the best thing going. So I am wondering if you are getting the same reaction that we were getting at that time.

Mr. SHANE. That was the reaction initially. Since that time I think we have found that development of their technology is on a slower track than the French anticipated at first. That is an impressionistic answer. I am not sure I know exactly what the state of their development is. As you know, we have ordered six TNA machines and we have identified six locations for the deployment of those machines; France is not one of them. So it is not a very live issue right now with the French. Until we are satisfied ourselves that this technology is the kind of technology that we want to deploy in a much bigger way, I don't think we will join issue with the French any further on that. If, indeed, they can come up with a superior means of detecting explosives, I think we would all be delighted to see it.

Mr. OBERSTAR. If the gentleman would yield, I would elaborate on that point. The French Government has encouraged its principal developer, a private sector company, to join with a U.S. firm, and that has been done. A joint venture, a 50-50 basis joint venture has been formed between a French company and a U.S. California-based company to develop what they call "Fast Neutron" technology and the two companies are jointly developing this technology. But in contrast to the statement made by French authorities to us during our subcommittee meeting with them over a year and a half ago that they would be ready with this technology in a year——

Mr. **Inhofe**. That's right. I remember that.

Mr. **Oberstar**. It is a year and a half now and they are finding it much more difficult to achieve that technological breakthrough.

Mr. **Inhofe**. Okay. Thank you, Mr. Chairman.

I would now like to have you move to the other area that I brought up, and that is the controllers problem over there, and maybe specifically one other of area of that and that is a uniformity that we hope and were told would come. I am a pilot and I know what it is like to piddle around in that stuff. I think about some of our pilots that are trained here, are used to our system here, they know how to declare emergencies, they know how they can penetrate a system and it is totally different over there right now. It seemed that we were trying to say that, well, we'll come up with some uniform plan, and that was our nice way of saying we're doing it better than you are doing it, you ought to be copying us because we are doing a lot better in that job of controlling air traffic here than they are.

Granted, they have a problem when you take the number of airplanes and the smallness of Europe and the different languages and all that, there are some other problems there. But do you think that we will achieve any type of uniformity when we get to any point along here in controlling air traffic between us and the European traffic, and, if so, will it emulate ours more so that theirs can be improved?

Mr. **Shane**. Again, I am afraid I am not in a position to make a very clear or encouraging prediction about that. We have certainly spent a lot of time talking to the Europeans about this problem. If there is one source of encouragement, it is that the European carriers themselves are absolutely frustrated with the European system. It is killing to European carriers to spend as much time circling airports in Europe as they do. It has gotten so bad that it does, indeed, spill over to our market in peak traffic times. The U.S. carriers flying out of Europe can no longer rely on their ability to arrive in a U.S. airport at a particular time. Those delays cascade into our system because those airplanes get held up and they have to go to other places. So we have brought this problem to the attention of the Europeans very specifically just in terms of the damage that it is doing to the reliability of our own system.

They have something like 22 centers in Europe. Planes are handed off from one center to another almost every few minutes. It is an absolutely backward system, and I have been told that by chief executive officers of European airlines. I am not saying anything that the European airline managers would not agree with.

I think if there is going to be progress, that progress will come from the pressure which European carriers bring to bear on those who are running those systems. I am afraid that I am just not in a position to make a prediction as to how fast they are going to produce those kinds of improvements.

Mr. **Inhofe**. I think maybe that is just something to be looking for. People here complain in congested areas about ramp time and I always respond to them that it could be worse; you could be in holding pattern time during that time. It works out about that same time frame, except they do it up there and we do it down here. So I am hoping that we can be looking toward an improvement as we move along there.

Mr. **SHANE**. Well, that's an example of one of the many things that, even given their present system, they could begin to do to improve the situation. The FAA specifically adopted flow control to avoid the spectre of airplanes circling endlessly. Nobody is allowed to take off now unless there is a chance to land and a reliable place to land.

Mr. **INHOFE**. That's right.

Mr. **SHANE**. The Europeans could do the same thing. European air traffic controllers handle fewer airplanes per person than U.S. air traffic controllers do. Separation standards are very different and much less efficient than our own. We think there is room for improvement in ours; but they haven't in most places in Europe, as I understand it, even achieved the efficiencies that we have. So even accepting the basic structure of the system, we think that there are enormous improvements that can be built in. Again, they are all sovereign governments and they are going to have to make those decisions for themselves. We just urge them at every opportunity to do so as quickly as possible because, you are absolutely right, it goes to the same question we were discussing earlier—airport capacity. Without these infrastructure improvements, all the vaunted talk of liberalization of the European market is going to go nowhere because you can't liberalize an absolutely saturated system.

Mr. **INHOFE**. It is a big problem and we wish you the best of luck.

Mr. **SHANE**. Thank you.

Mr. **OBERSTAR**. The gentleman's time has expired.

Before I recognize the gentleman from California, I have just an observation. Europe has one-fourth the air space of the United States and twice as many air traffic control centers and an antiquated technology that is older than some of the old Civil Aviation Authority equipment in place in the United States before the National Aerospace System plan. Europe has developed Euro-control similar to FAA central flow control, but it is not as effective as flow control in the United States. Which raises the question the gentleman from Oklahoma was pressing, and that is when we gain rights to European airports, if their air traffic control system is antiquated, inefficient, and controllers have to hand off by telephone to other controllers in other countries and not by computer, and the aircraft are put in holding patterns in the skies, all of that diminishes the value of the right that we gain through the very able negotiations that you conduct. And those carriers then have the rights to the United States with all of our efficiencies, our $25 billion modernization of the air traffic control system, and all the benefits of airport capacity improvements. They gain much more valuable rights in the United States than we gain in their countries.

The gentleman from California, Mr. Packard.

Mr. **PACKARD**. Thank you, Mr. Chairman.

Mr. Shane, the International Air Transport Competition Act of 1980, it has given rather significant authority to the DOT to close down foreign airlines if they mistreat the United States in our aviation activities. Has that been an effective law; have we used it very much?

Mr. **Shane**. I think it has been an extremely effective law and we have used it; we have used it a lot. We reviewed our usage of the Act recently and I think we have had something like a dozen or 14 specific cases; complaints brought by U.S. air carriers against various forms of discrimination that they have encountered in foreign operations.

The law is a tough law. It puts the Department of Transportation's feet to the fire by establishing very firm deadlines for taking action. It requires that we try to work things out through negotiations or consultations before actually retaliating, and we have taken that very seriously. The foreign government always understands that the Department of Transportation at the end of the day is going to have no choice about retaliating if we don't get the problem solved. I think it is a beautiful formula. It has worked time and time again. We have demonstrated our willingness to retaliate. As I say, we would not have any choice if, indeed, we weren't able to rectify a discrimination through negotiations.

We have solved a lot of problems through the existence of that Act. I would even say that we have solved a lot more problems than the ones that surfaced in the context of formal complaints. The very existence of the Act, I think, serves to enhance the effectiveness of the negotiating process. When somebody complains to the Department of Transportation or to the State Department about a discrimination and we begin informal consultations, long before anybody files a formal complaint under the 1980 statute, our counterparts abroad understand that this is the beginning of a process that will almost certainly culminate in that formal process and, therefore, almost certainly culminate in a real tit-for-tat exchange of retaliation if we don't get the problem solved. I am happy to report that on balance we have solved the vast majority, if not all of those problems, through that process.

I don't have for you a number of cases specifically in which we have actually had to retaliate. My inclination is to think that we have actually not had to because we have gotten the problem solved before it was necessary, but I will correct myself later on the record about that.

[The following was received from Mr. Shane:]

After further review, I confirm my testimony that the Department has not actually had to implement retaliatory measures against a foreign carrier to resolve a discrimination problem under the International Air Transportation Fair Competitive Practices Act. However, in three cases, two involving Japan and one involving the United Kingdom, we or our predecessor, the Civil Aeronautics Board, did adopt retaliatory sanctions. The threat of those sanctions promoted resolution or amelioration of the problems in at least two of these cases.

Specifically, in 1981, the Japanese government refused to honor United Air Lines' designation to serve the Seattle/Portland-Tokyo route. After attempts to resolve the dispute through intergovernmental negotiations failed, the CAB announced several steps, the most important of which was an order that would have curtailed Japan Air Lines' operating authority to the United States. The order was subject to Presidential approval. Since negotiations with Japan had already been scheduled, the CAB requested that the President defer action on the order pending those discussions. Subsequently, the United States and Japan reached an agreement which provided for Japanese approval of United's Seattle/Portland-Tokyo services.

In another case involving Japan, The Flying Tiger Line (now Federal Express), complained against the Japanese government's refusal to accord Flying Tiger cargo space to implement its license to conduct third-party cargo handling operations. In response, the Department determined to deny the Japanese cargo carrier, Nippon Cargo Airlines, eligibility to increase its cargo operations under a 1985 Memorandum of Consultations. Federal Express subsequently acquired Flying Tiger and withdrew the complaint before Nippon Cargo was actually denied any frequency increases.

In a 1986 case, The Flying Tiger Line complained against announced United Kingdom regulations that would have adversely affected U.S. cargo carriers at London's Heathrow Airport. The Department determined to restrict the operations of United Kingdom carriers at high density U.S. airports if the United Kingdom implemented the regulations. Since the United Kingdom has not restricted U.S. carrier cargo operations under their rules, our announced sanction has never been triggered.

In several other cases, the Department did not actually adopt sanctions, but did institute procedures to enable it to take retaliatory action if necessary. Two of these cases involved complaints against foreign government refusals to honor U.S. carrier designations. The Department required the foreign carriers to file their U.S. schedules with the Department and put the carriers on notice of its intent to reduce their U.S. services if the complaints were not resolved. In neither case did the Department have to curtail the foreign carrier services, since each case saw the U.S. carrier receive operating authority.

In three other cases, U.S. carriers complained against foreign carrier CRS practices. In each case the Department proposed sanctions that would have limited the sale and marketing of the foreign carrier's services through U.S.-based computer reservation systems. In each case the threat of such remedial actions promoted intercarrier resolutions to the complaints, and no sanctions were ever implemented.

Mr. PACKARD. What kind of flexibility do you have in imposing the retaliations? Let me take, for example, Japan, where they have prevented UPS from slots. Are you able to only retaliate in terms of not allowing Japan to have slots at one of our airports for cargo carrying, or can you apply that to passenger carrying?

Mr. SHANE. Basically, the answer to that question is simply a function of our calculation of the economic benefits that were extended to the other country in return for the economic benefits which a U.S. carrier is not enjoying as a result of discrimination. So at the negotiations you would look at the agreement and see what the balance of benefits that you anticipated when you signed it was and, if indeed the benefits that we expected aren't materializing, then you would just simply withhold the benefits that the other side expected. I don't think there is any—there is no formula that says that if it is a cargo problem you have got to hit them on cargo, or if it is slot problem you have to take away slots. By and large, we try to stay within the general concept of proportionate countermeasures. That's a term from international law that suggests that you shouldn't do something to the other side that is somehow disproportionate in terms of the harm that you are suffering. You try to make it an equivalent economic harm, but it doesn't necessarily have to be the same specific element of the service.

Mr. PACKARD. In the case of the UPS slots at Tokyo, would we have been ill-advised to have, for example, prevented Japanese airlines from having landing slots at O'Hare; or would that have been an excessive response?

Mr. SHANE. I looked at that possibility very specifically, Congressman Packard, and the problem I found with it was that we just didn't know how to do it. Because of the nature of trans-pacific flights, the arrival times that both JAL and NCA were seeking—we can provide this for you on the record—were not very far away from those times of day or night at Chicago O'Hare which were not controlled. Right now our wherewithal to deal with slots extends just to those slots which we actually regulate through the high density rule. So to tell them that they wouldn't be able to have a slot that we did control, that is to say in the hours that we control slots, would have just been to say that, of course, if you come in a couple hours later in the uncontrolled times, we won't have any control over you. We would have basically given away our ability to retaliate effectively.

The slot mechanism just didn't work as a retaliatory mechanism. That's why we just decided to withhold the authority altogether.

Mr. PACKARD. You did mention in your testimony that you have withheld cargo carrying slots to the Japanese, did you not? I thought I heard that.

Mr. SHANE. No, what I said was that we have simply withheld their operating authority; the authority of JAL and NCA to operate all cargo flights to Chicago.

Mr. PACKARD. I see.

Mr. SHANE. Which was a specific benefit extended to Japan under the same agreement that enabled us to designate UPS for service to Tokyo.

Mr. PACKARD. So that withholding of those slots was in response to their withholding of slots to UPS?

Mr. SHANE. Yes. I should really clarify. They are not withholding slots from UPS. They have granted the number of slots which UPS asked for. The problem is—and I don't mean to understate at all the very real problem that exists at Narita—the problem was that the Japanese gave UPS slots which were simply not competitive in terms of the operating situation at Narita. Instead of the evening slots which they would have to have in order to provide an attractive service to the customers that are in Tokyo, they had slots the next morning. All of the competitors' flights would have left, all of the cargo would be on the competitors' flights by virtue of the fact that they were leaving the night before. Consequently those slots simply didn't work as an effective competitive device. Therefore, what we have said is, we know you have given them the right number of slots, but you are not extending to UPS something else that is guaranteed in the bilateral agreement—a fair and equal opportunity to compete with both Japan Airlines and NCA.

Mr. PACKARD. Thank you, Mr. Chairman.

Mr. OBERSTAR. Yes, on that latter point, certainly we have had enough experience with the Japanese to know how they have manipulated the "doing business" issues in such a way as to undermine the value of the rights that they negotiated for our carriers, this is another example of it. They will state in their own defense that they have all these problems at Narita Airport, the noise, capacity, congestion, and can't add more. But why did they negotiate in the first place? They knew very well that for the valuable right to cargo in Japan, U.S. carriers, which operate at night in the United States, and to accommodate the slots that the Japanese were offering UPS, UPS would have to convert to a daytime operation in the U.S., and totally turn their business around. It can't be done; that's just not the nature of that kind of freight business. They know that. They know it very well. We have been through it on the self-handling issue, we have been through that earlier on customs and on gates and positions with the Koreans, where they give us something that is way at the end of the airport. Over and over again, it is just very, very frustrating and you have got to be firm with them. The only way they understand is if we negotiate something very valuable to them in the United States, and require them to give us something equally valuable in their country, so the trade will be on a level basis. Hang firm.

Let me walk you through a few thoughts now on some broader issues. I say with respect to the Canada issue, this subcommittee is working out an exchange with Canada. I am inviting members of the subcommittee and our professional staff to join me in a session in Ottawa and hope, in early December, to have an exchange with members of the Canadian Parliament and their Transport Minister, to further explore these matters.

You pointed to the growth in the U.S. market share of international airline traffic and you said it was attributable to our pro-competitive policies. Then you also said in many international markets a number of the problems that we overcame with deregulation still remain. So I am not quite sure how you link pro-competition policy in the United States, deregulation, to growth in U.S. market share in international airline traffic. What is that particular linkage?

Mr. SHANE. The comparison that we draw is between bilateral markets—that is to say foreign markets—markets between the United States and those foreign countries that have worked out with us liberal or deregulated bilateral agreements as compared to those which have been relatively more restrictive in their policies toward us. So we are really looking not so much at the domestic market which is deregulated, or a foreign domestic market, if you will; we are looking at the markets for international air transportation between the United States and particular foreign countries.

Where we have seen the U.S. carriers do best are those markets which we have been able to liberalize through the bilateral negotiating process, where agreements diminish the wherewithal of either the United States Government or a foreign government to regulate prices, or capacity, or the number of airlines in the market, or schedules, or so forth. That's where we do best. Therefore, our policy, it seems to me, must be to continue to try to establish the kinds of conditions in which our carriers do succeed best, and those are the liberal markets. I think that's the linkage I was trying to draw.

Mr. OBERSTAR. Your point by point discussion of various countries and their relative position in importance dollar-wise or otherwise, trade with the U.S. underscores the reality that a number of obstacles and impediments remain to a free and open market. That takes me to the next point that Secretary Skinner has pursued, as you said, "Open Skies" aviation agreements. Is this much different than policy pursued by other secretaries, going back to the Carter Administration even?

Mr. SHANE. Oh, it is. I don't think the United States has ever offered all U.S. cities to any foreign carrier. That is what Secretary Skinner has done. He has said if you are prepared to simply back away from the regulation of U.S. airline services to your country entirely, then your carriers—whether it is Lufthansa, or British Airways, or Virgin Atlantic, or Air France—may fly to any and all cities in the United States. That is a dramatic, watershed departure from our past negotiating policy under any other Administration.

Mr. OBERSTAR. So it is in the completeness of the Secretary's offer is how it differs from the past?

Mr. SHANE. We have always sought liberal agreements——

Mr. OBERSTAR. We have negotiated incrementally toward that objective, now the Secretary is saying take a blanket approach to it overall.

Mr. SHANE. Mr. Chairman, even in our efforts to negotiate incrementally toward that objective, I don't think any one else, any previous Secretary of Transportation had ever envisioned that at the end of the process we would offer the entire United States to the foreign carrier. I mean, we have, just to take some examples, completely liberalized bilateral agreements with Thailand, with Korea, with Taiwan, with Singapore. Each of the foreign carriers involved in those agreements has a limited number of points in the United States. Even where we got a liberal agreement, in other words, with a foreign government, at least in past Administrations, we nevertheless kept a very close count of the cities in the United States that they would be entitled to fly to.

What we are saying now, at least in the context of these major transatlantic markets—the U.K., France, and Germany, in particular—is that if you three, or any one of you, are prepared to sit down and simply deregulate the bilateral market between your country and ours, then we have no interest in telling you which cities in the United States you can fly to any longer; you can choose from any of them.

Mr. OBERSTAR. They are having a hard time digesting that proposition.

Mr. SHANE. Precisely. And it is a tribute, I must say a left-handed tribute, to the strength and competitiveness of the U.S. carriers that they will have to fight on their own home turf. I think it is fear of their possible inability to compete successfully against the kinds of lean, mean carriers that our deregulated market has spawned that has created this reluctance to embrace the kinds of agreement, I should say ironically, which these very governments have clamored for for years. I mean we really thought we were simply saying yes to something that they had all been seeking. So to hear them say, "Not so fast; we have to think about that," is a little disappointing to us.

Mr. OBERSTAR. Well, it is. I think you are moving in the right direction in pressing them properly and appropriately. I urge you to continue that effort.

The next point I want to get to is that it seems to me that cross-investment has become the current wave and may be the wave of the future of foreign carriers investing in other foreign carriers. We may be moving to a regime where we have a few JAL-type carriers, one massive huge carrier somewhat more or less supported by government financing and policies that favor that national carrier with obvious implications for U.S. trade. What do you see as the shape and structure of the airline industry worldwide over the next decade, and what policies are you shaping to meet that challenge?

Mr. SHANE. Well, there is a tension now between what you see as a real desire on the part of airline managements around the world to establish those cross-border linkages, thereby creating global airlines in the true sense of the term, and the very structure of the way we establish these markets on the basis, as you say, of government-to-government bilateral negotiations. You can't have a bilateral negotiation that's any good unless you understand who the beneficiaries of the negotiating process are going to be. That is to say you have to understand what the flag of the carriers on both ends of the market will be.

If you start having cross-border investments that begin to internationalize or multinationalize airlines in a way that goes a little further than what you have seen up to now, at least in most places, it seems to me that is going inevitably to call into question what the negotiating process is all about. We have very strict citizenship rules in our country. When we send an airline to a foreign country, that country understands that it is an airline of the United States, it is a U.S. citizen corporation. If it gets to the point where the United States is no longer able to tell what the citizenship of a carrier that is flying to the United States is because of cross-border investments in Europe or anywhere else, we are going to have to try to figure out for ourselves, now wait a minute, who exactly did we mean to extend these economic benefits to.

Mr. **OBERSTAR**. Exactly.

Mr. **SHANE**. If we have a country that has not given us very many rights to fly to its territory but they begin themselves to enjoy enormous economic rights by virtue of investments in the national carrier of a country that has been fairly liberal with us, then all of a sudden it seems to me our wherewithal to negotiate effectively with that more restrictive country has been seriously compromised.

Mr. **OBERSTAR**. That is a matter of very great concern to me. I am glad that you have underscored that and elaborated on it because I see this development occurring at an even greater pace and I see also the potential for swallowing up of U.S. carriers, some of the smaller ones that may have financial problems; and, in particular, in today's economic climate what this means over the next ten years as foreign carriers see an opportunity to get into our marketplace with other devices.

Mr. **SHANE**. But then you put your finger, Mr. Chairman, on the conundrum, because then you have airlines around the world that have access to capital from all sources, domestic and foreign. The tension that we're trying to resolve is the need to ensure that U.S. carriers have access to that same capital with as much liberality as their competitors have—because, after all, competition among airlines is in many ways competition for capital—without, of course, divesting ourselves of the wherewithal to say that these are, indeed, U.S. citizen corporations. That tension is a tension that you see us trying to resolve in the context of these cases that we were referring to earlier.

Mr. **OBERSTAR**. Thank you. I'm going to have to break now for a vote on the House floor and come back to review in a little more detail the European negotiations and trade issues and then the Canada question. I have some labor impact questions that I want to explore with you. And depending on who else comes back, we may conclude after that.

[Recess.]

Mr. **OBERSTAR**. The subcommittee will be in order.

Following up on the last point that I raised, that of ownership, you said that you're sticking with the U.S. statutory requirements, that United States air carriers must meet certain citizenship standards. What changes might be anticipated in the 1990s in those standards?

Mr. **SHANE**. Seems to me the answer to that question could make a lot of headlines. [Laughter.]

Mr. **OBERSTAR**. The question doesn't make headlines; the answer will.

Mr. **SHANE**. Well, I hope it won't. There is certainly, as I indicated before, and as you indicated, Mr. Chairman, increasing pressure for cross-border linkages. Airlines around the world including our own understand that their ability to compete successfully in the world in the future is going to require the broadest possible scope of coverage and the broadest possible market presence. You have already begun to see some dramatic movements in that direction through cross-border investments, market joint ventures, and similar devices that we referred to earlier.

Right now, I believe that our law does, in fact, permit U.S. carriers to access foreign capital markets successfully. It is not the intention of our law or certainly of our policy to discourage the access that U.S. carriers enjoy to foreign capital markets. What our law is designed to discourage is the actual taking over and controlling of U.S. carriers by foreign citizens. It's conceivable, and I say it's just conceivable in the longer term, that if the cross-border activity that we see the beginnings of right now suddenly accelerated and ultimately culminated in the diminution in the importance of the concept of national flag in the airline business, I suppose at that point—and I don't see that happening anytime soon, if ever—at that point, I suppose the United States might want to reexamine whether or not there was continued relevance to the citizenship requirement. But that would be a very large departure from not only the way the United States operates now in international aviation; it would be an enormous departure from the way the rest of the world operates.

So I'm not here predicting that that's going to happen anytime soon. Indeed, it may not happen in our lifetime. That's the only, if I may, the only trigger it seems to me that is likely to produce any dramatic departure from our citizenship requirements.

Mr. OBERSTAR. Is there a chicken and egg proposition here that certain things must precede other things? That the regime governing aviation trade, marketing of the aviation product must change in any country with whom we might change our ownership and citizenship standards before we would change those standards?

Mr. SHANE. To me, the first step would probably have to be a restructuring of the way we establish the markets. Just to take Europe as an example, again, if indeed Europe became a single market and they established a policy which enabled the European community to negotiate with the United States as a single unit, at that point I guess it would be less important to us what the flag of a particular European airline was. That is to say, if it became one country for negotiating purposes, then they would all be just EC carriers as far as we were concerned.

If, then, that process of integration expanded so that the European Community embraced perhaps non-European countries and you had a broader integrated market, again, the concept of flag would be less important and the whole process of establishing markets would begin to change.

If you finally got away altogether from negotiating the opening up of particular routes on a bilateral basis, it's arguable that there would no longer be a very strong interest on the part of any government in worrying about the particular nationality of the companies that were providing transportation to and from its territory. We would always worry about the success of U.S. airline companies, but all of our experience has taught us that the more liberal the market, the more successful our airline companies are. Our airlines do better, as you yourself said at the opening of the hearing, do better in liberal markets than in conservative markets. We have the strongest airline industry in the world, and the statistics that

I've shared with the Committee this morning are a clear demonstration of the extent to which we are more successful than anybody else. And it's reasonable to expect that if you did liberalize entirely all of the world's international aviation markets, our carriers would enjoy enormous success. As a matter of fact, I think you could say at that point, whenever that point comes, that the need to worry about the flag on the tail of airplanes flying around the United States or to and from the United States would no longer be as important as it is today when we're negotiating all of these markets on a bilateral basis.

But I want to underscore that that is what you might call "far-out" thinking. I don't see it emerging anytime soon. I'm not proposing that we have any immediate plans to suggest any changes in the present law. We think that the law does accommodate foreign investment in U.S. airlines; it accommodates it in a way that we think is appropriate. I don't know any reason why under present circumstances the U.S. Government would seek to propose changes at the moment.

Mr. **Oberstar**. Provided you're more attentive to the matter of control which may translate to less than 25 percent ownership.

Mr. **Shane**. Well, it seems to me that control is only partly a function of the amount of voting stock which a foreign entity holds. Indeed, that is your point about the SAS Continental transaction, notwithstanding the fact that they control something like 18 percent of voting power which normally would not be a way of establishing control. Mr. Chairman, it's your position that SAS might well be in a position to establish that control. The Department of Transportation has said that by virtue of the reporting requirements, by virtue of recusals and other conditions established for the SAS participants in Continental, we think that there will not be control and, indeed, we have the wherewithal to keep our eye on the company and make sure that that control never emerges.

I fully respect your position on the thing, and we do want to keep our eye on it. We just want to learn as much as possible about these transactions by watching the way they work in the aftermath of our decisions.

Mr. **Oberstar**. I think basically the problem is not quite so much the Department's judgment on the matter as that it is interpreting very old law that does not reflect the realities of today's marketplace. And, yet, I think the Department is doing as good a job under that act, although I would have gone further, as I said. I think we have to recognize when there is no entity that owns more than three percent of AT&T stock, if somebody suddenly buys five percent, they become a very big player in that corporation's decisions.

Let's spend a few moments on Europe. On integration in Europe there are opportunities and problems as you have said. One of the problems is that the EC has not resolved the question of cabotage to the best of my knowledge. In discussions that our subcommittee members had with Mr. Von Meert in Europe over a year ago and subsequent meetings with EC representatives who have come to the United States, we've had further discussions including Mr. Sorenson from the EC. Do you have any sense of whether Europe is on the verge of resolving—by Europe, I mean the EC—resolving the question of how trade among member nations will be treated in the post 1992 era?

Mr. **SHANE**. I don't have any specific knowledge of how close they are to resolving the cabotage question; and certainly there are other questions that are arguably of even greater interest to us. For example, I don't know whether they have agreed with each other that they will share each other's gateways. That is to say, will Air France be able to use London as a gateway for services to the United States? They need our permission, of course, to do that. That would be arguably the kind of question that would come up in a negotiation with the EC, but I don't even know today whether or not that is the kind of exchange with each other that they envision becoming part of the ultimate package.

One would expect that cabotage would be a natural element in any truly integrated market. It may be that they are planning to phase in what we would think of as true cabotage over a period of time, as they have phased in so many other aspects of the liberalization of the market, but I just don't know—I'd be happy to report back to the Committee if we are able to get any clearer definition of what, in fact, is anticipated.

[The following was received from Mr. Shane:]

On review, it appears that the issue of true cabotage is still an open question in the Community. The Commission's package for the second stage of liberalization included a proposal for some limited cabotage for EC carriers within other EC countries. The Commission proposed to allow carriage of cabotage traffic on flights originating or terminating in the carrier's homeland, in other words as an extension of international services within the EC, provided that only 30 percent of the capacity on the extension leg was used to carry cabotage traffic. However, the member states were not yet prepared to accept any relaxation of cabotage restrictions, and the Commission's proposal was dropped from the phase-two package eventually adopted by the Council of Ministers in June 1990.

Mr. **OBERSTAR**. It seems to me that's a very difficult question for the Europeans to resolve and it impinges directly on our trade because if, indeed, Europe becomes a single market and a French carrier can move German passengers from German soil to Italian soil, Italian passengers elsewhere, then there are big implications for our bilaterals which may have to be renegotiated altogether.

Mr. **SHANE**. Yes, I think there are big implications for the very shape of the European market. After all, what we saw happen in the United States when we liberalized—that is, to say, deregulated the domestic market here was that we saw a number of communities, many communities around the country that had never had any prayer of supporting transatlantic air service suddenly turning into hubs by virtue of U.S. carrier decisions, suddenly becoming important collection and distribution points for airline operations, and suddenly, indeed, becoming transatlantic gateways. I think of Charlotte as the classic example. If anybody had suggested to you in 1978 that Charlotte would support daily non-stop service to London, I think you wouldn't have been taken very seriously. The fact is that they have it today. Raleigh-Durham supports service to France I believe every day of the week.

We've had that phenomenon in our market; it's reasonable to expect that you will have a similar phenomenon in the European market by virtue of what airlines are able to do in a liberalized environment. That, I think is going to translate into some very different kinds of aspirations on the part of U.S. carriers for services to Europe. That will make for a very interesting negotiation. We will finally at long last need gateways in Europe that we don't currently seek. We've been serving the principal European gateways from time immemorial, from the beginning of the bilateral negotiating process, at least from the forties. As a result, there seems to be a real tension in our negotiations because U.S. carriers for the most part—there are some exceptions to this, of course—but for the most part, they feel that they already have access to the markets that they wish to serve. If by virtue of liberalization new markets emerge, new real gateways emerge within Europe, then it seems to me that there ought to be an interesting negotiation between the United States and the EC.

Mr. OBERSTAR. For the time being then, you anticipate continuing to negotiate or conduct talks with our European partners in the context of existing bilaterals rather than in the context of some yet-to-be-seen broader regime?

Mr. SHANE. Yes, for as long as it remains fruitful to do so. Of course in their anticipation of an integrated market, they're becoming difficult negotiating partners from time to time. Because no one in Europe is yet in a position to predict exactly what the outcome of the integration of the EC will be, there's a certain reluctance that I've detected to enter into dramatic new arrangements with the United States. That may very well be one of the factors which resulted in none of the partners that we extended the open skies offer to deciding to accept it. I think they're unwilling to make important new deals with the United States in the context of the kind of uncertainty that exists in Europe right now.

Mr. OBERSTAR. Now, moving on to computer reservation systems which are a matter of some very great concern and growing concern—in fact, there is a recent European civil aviation organization publication that addresses this matter of these two huge international systems in Europe, Galileo and Amadeus, which you've addressed in your testimony. How do these two European computer reservation systems, affect our trade relations with the current EC and what changes might we anticipate in post-'92?

Mr. SHANE. It's important to distinguish between competition among airlines for passengers and competition between different computer reservation systems.

Let me just talk first about the competition between airlines. It seems to me that we can't do anything but benefit from the very sophistication of the systems that are now going to be the principal systems in Europe. What we had for many years were systems run by national carriers in each country which, not because they sought to discriminate against U.S. or any foreign carrier, but just because of the primitive nature of those systems, made it very difficult for U.S. carriers to market effectively to foreign nationals within Europe.

I think we must ultimately benefit from the fact that the Galileo and Amadeus systems are world-class systems; they take advantage of the best software available, in some cases U.S. software, and it will make, it seems to me, for a much more effective marketing effort on the part of all of the carriers that participate in those systems. Because the systems are inherently multi-carrier systems, I would expect them to get away from the kinds of occasionally intentional discrimination in favor of national carriers that we have seen from the previous systems that were indeed owned and operated by national carriers.

To the extent that we see rudiments of that kind of discrimination in favor of national carriers, of course, we'll find ourselves in a bilateral dispute. And, in fact, we've been in those disputes from time to time, and I think the Chairman and the subcommittee know that we have taken those very seriously. We've resolved a number of problems through the IATCA process on behalf of U.S. carriers seeking to market more effectively both their airline systems and their CRS systems within Europe.

Turning then to competition between computer reservation systems themselves, our position has been, as I believe the Chairman knows, that the fair and equal opportunity to compete required in all of our bilateral agreements with our European partners embodies an obligation by foreign countries to accommodate the full and free marketing of U.S. vendor-owned computer reservation systems within European markets. We first got into a dispute on that issue with the U.K. when the American SABRE System found difficulty in getting deployed within U.K. territory. We ended up in a formal dispute about that. At long last American and British Airways were able to work out an arrangement in which, indeed, American could deploy the SABRE system to its satisfaction.

A similar program inhibited American from deploying SABRE within Spain, another IATCA case. We ended up with another success at the end of the day.

So we've taken the ability of U.S. airlines, U.S.-CRS vendors, to deploy their CRS systems within Europe very seriously as a bilateral aviation issue and we'll continue to do so.

I think it's possible to define that issue as a trade issue. I mean, it's conceivable that you could treat it as a telecommunications issue and take it up within trade negotiations rather than aviation negotiations. My position has been, and the Department of Transportation's position has always been, that we ought to keep it within the framework of our bilateral aviation negotiations. Computer reservation systems are so essential to the marketing of air transportation today—I used to say 80 percent was the number of tickets driven by CRS; it may be higher today, it may be closer to 100 percent for all I know—it's so essential a part of the process that we need to keep it within the overall exchange of rights, and those rights ought to include the aviation services themselves.

Mr. Oberstar. Very good. And I fully agree and I think this committee agrees very strongly that on that score that CRS issues should be kept within the context of the bilaterals, and that brings us to GATT and the very strong position this Committee has taken on keeping aviation out of the effort that was announced by our trade representative to put it into the context of services under GATT which would have undermined it seemed to us the strength of our bilaterals. What is the current state of that issue?

Mr. Shane. I guess I should say as a preliminary matter that the negotiations thus far have been about a so-called framework agreement—that is to say, the framework within which different sectors would be discussed. Our position thus far, in fact it remains our position today, has been that there ought to be the wherewithal for different parties to any new GATT agreement that emerges from this round to exclude particular sectors. That is, if you have the ability to exclude particular sectors, then it would be open to the parties of this agreement to exclude, for example, aviation.

We don't know exactly what the final result of the negotiation on the framework agreement will be. In working very closely with our negotiators within the U.S. Trade Representative's office, I think I can say with some confidence based not only on what the United States' position has been, but also the position that we begin to see emerging from many of our partners in those negotiations—other governments—that either we will have the wherewithal to exclude whole sectors such as aviation; or if we don't have the formal ability to exclude a whole sector, at the very least there will not be more than the most basic obligations applicable to sectors like transportation—aviation in particular.

In either case, it seems to me that the likely outcome will be substantive exclusion of aviation services from the full application of GATT obligations which I believe is consistent with the position that the Chairman has outlined.

Mr. OBERSTAR. Thank you. At this point I would ask unanimous consent to include in the hearing record the committee letter of August 1, 1990 to Secretary Skinner and the letter the committee received yesterday from Secretary Skinner in response to our August inquiry on this point.

[The referenced letters follows:]

GLENN M. ANDERSON, CALIFORNIA, CHAIRMAN

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MEL HANCOCK, MISSOURI
CHRISTOPHER COX, CALIFORNIA
SUSAN MOLINARI, NEW YORK

Committee on Public Works and Transportation
One Hundred First Congress
U.S. House of Representatives
Room 2165, Rayburn House Office Building
Washington, DC 20515
TELEPHONE: AREA CODE 202, 225-4472

August 1, 1990

Honorable Samuel K. Skinner
Secretary
Department of Transportation
400 7th Street. SW
Ste. 10200
Washington, D.C. 20590

Dear Sam:

We are writing to urge that airline services be totally excluded from a General Agreement on Trade in Services now under negotiation as part of the Uruguay Round of trade talks.

We have had concerns for some time over the inclusion of airline services. Inclusion would undermine what has been generally regarded as a good, working system to enhance civil aviation opportunities for United States air carriers and travellers and to resolve disputes between the United States and our foreign aviation partners.

Last November, the Subcommittee on Aviation held hearings on whether airline services should be included. Subsequent to that hearing, thirty-seven Committee Members, from both sides of the aisle, communicated their strong concerns about inclusion in a letter to Ambassador Hills. Last March, H.Con. Res 280 was introduced expressing the sense of the Congress that airline services should not be included in a services agreement. That Resolution has 179 cosponsors indicating broad House support for exclusion. For your information and reference, I am enclosing the hearing publication, a copy of our letter to Ambassador Hills, and a copy of H.Con. Res 280.

Much of the policy debate within the U.S. Government on whether to include airline services in this agreement has been non-public, making it somewhat difficult to discern exactly where the debate rests at any given time. However, it appears to us that the U.S. Government may be moving to propose or accept the inclusion of airline services in a General Agreement on Trade in Services, with inclusion limited to what have become known as the "doing business" issues. Our understanding is that airline routes and rates would continue to be negotiated bilaterally.

Excluding routes and rates while including "doing business" issues, would seem to provide a compromise between those who favor exclusion of airline services and those who seek universal coverage of all service sectors in a services agreement. In our opinion, this arrangement is a compromise in form only; it does not assuage our concerns about including any aspect of airline services in an agreement. The "compromise" would be detrimental to the interests of the U.S. traveling public, U.S. airlines, and U.S. workers.

To separate routes and rates from the "doing business" issues would naively assume that airline route rights can be negotiated and that rate regimes established with no consideration as to how these agreements are implemented. Over the past several years, the Congress has come to appreciate that how our bilateral agreements are implemented is just as important as the agreements themselves. If a U.S. carrier receives rights to serve a new route, but is unable to obtain a landing slot; or is charged discriminatory landing fees; or is not permitted to market its services to the public; or must depend on competing foreign carriers to provide ground service, then these new rights become severely diminished if not meaningless. We are very pleased that over the past several years, the Department has come to recognize this when it sits down with foreign governments to discuss civil aviation matters. We would view divorcing routes and rates from "doing business" issues as a complete reversal of the progress we have begun to achieve bilaterally in recent years.

Further, by moving "doing business" issues under a General Agreement on Trade in Services framework and out of the bilateral process, the U.S. would be diminishing considerably its negotiating strength to resolve these vexing and ubiquitous problems of conducting business abroad. Frequently, when U.S. interests have a problem with such mundane matters as adequate ticket counter space, ground handling arrangements, landing fees, which airport charter flights will use, and computer reservation system regulations, the U.S. is able to resolve these problems because a foreign carrier wants to initiate new service to the United States. Resolution or mitigation of U.S. carriers' problems often come because the U.S. Government is able to reward good behavior with something very valuable, the right to fly to the United States. If "doing business" issues are removed from the bilateral process, the U.S.' natural negotiating strength and leverage would not be able to be used effectively to resolve these very real problems.

For these reasons, we urge you to involve yourself directly in the formulation of the U.S. Government position for the rounds of talks to take place later this Fall. And of course, we urge that you work to see that airline services in all their aspects, including the integral "doing business" issues, are excluded from the General Agreement on Trade in Services.

Finally, we want to let you know of planned hearings by the Subcommittee on Aviation this Fall to conduct a general review of U.S. international aviation policy. We take this opportunity to extend you an invitation to make a presentation on the future direction of U.S. international aviation policy, including the impact of inclusion of any aspect of airline services in a services agreement, if that issue remains unresolved to our satisfaction at that point.

We would welcome the opportunity to discuss these issues with you further. Thank you for your attention and assistance in this very important matter.

Sincerely,

John Paul Hammerschmidt
JOHN PAUL HAMMERSCHMIDT
Ranking Republican Member
Committee on Public Works
and Transportation

Glenn M. Anderson
GLENN M. ANDERSON
Chairman
Committee on Public Works
and Transportation

Bill Clinger
WILLIAM F. CLINGER
Ranking Republican Member
Subcommittee on Aviation

Jim Oberstar
JAMES L. OBERSTAR
Chairman
Subcommittee on Aviation

THE SECRETARY OF TRANSPORTATION
WASHINGTON, D.C. 20590

October 9, 1990

The Honorable James L. Oberstar
Chairman, Subcommittee on Aviation
Committee on Public Works
and Transportation
House of Representatives
Washington, D.C. 20515-2308

Dear Mr. Chairman:

Thank you for your letter, cosigned by three of your Congressional colleagues, on excluding airline services from the Uruguay Round of the General Agreement on Tariffs and Trade (GATT). I welcome your views on this very important international transportation matter, and share your concern that the development of a GATT agreement on services must not inhibit further liberalization of civil aviation or hinder the timely and effective resolution of disputes with our aviation partners.

The Department of Transportation (DOT) has worked diligently to keep interested members of the airline community informed about progress on services negotiations in the GATT. We host and co-chair with the Office of the United States Trade Representative (USTR) regular briefings for the industry on developments in those talks. We also participate in similar briefings given to your staff. The DOT will continue these briefings until the Uruguay Round is completed. We anticipate a continued close working relationship with your subcommittee on this vital issue.

As you know, USTR has the lead role in the development and management of overall Administration trade policy. In recent months, USTR has been engaged within the GATT in a debate over the question of sector coverage (universal coverage versus the ability to exclude sectors in their entirety under special circumstances). The Department has been an active participant in that debate, and has made certain that the potential effects of a services agreement on the civil aviation industry--for both route/rates issues and doing business issues--have been fully explained to our trading partners.

Recent discussions among senior USTR and DOT staff have focused on how best to attain our overall objectives in the GATT services negotiations without compromising our objectives and negotiating environment for civil aviation. I am encouraged that we will be able to resolve this important question.

Be assured that I am giving this matter my close attention. Identical letters have been sent to the other cosigners of your letter.

Sincerely,

Samuel K. Skinner

Mr. **Oberstar**. We'll take a brief recess for this vote. With a few more questions, we'll conclude hopefully by 12:30.

[Recess.]

Mr. **Oberstar**. The subcommittee will come to order.

Switching oceans and trade regimes to cargo and Japan, bring me and the subcommittee up to date on the status of U.S.-Japanese all cargo service start-ups elaborating further beyond your statement under the bilateral with Japan and how that comports with the cargo trade policy.

Mr. **Shane**. You'll recall, Mr. Chairman, that we put a tremendous emphasis within the cargo trade policy, encouraged certainly by yourself and both subcommittees which you have chaired during that entire period, on the importance of ensuring that our all-cargo operators obtain in any exchange which extends all-cargo benefits to another country comparable benefits for themselves. We've taken that very seriously, specifically in the negotiation that we did in 1989 with the Japanese—or, I should say the agreement that resulted from negotiations we had done for several years ending in 1989.

We obtained a number of all-cargo opportunities. We obtained the right to have another U.S. all-cargo operator serving Tokyo from the United States. We obtained the ability for an incumbent all-cargo operator from the United States to serve a city other than Tokyo, in addition to Tokyo, as part of that agreement.

We exchanged for those rights opportunities for two Japanese carriers to previde all-cargo services to cities in the United States, including for the first time Chicago. The capacity restrictions imposed on Japanese carriers were such that we came away from the table feeling that, indeed, the all-cargo opportunities were very carefully balanced, almost calibrated, to ensure that they were approximately equivalent.

What happened in the aftermath of the agreement was that the Department of Transportation had the usual carrier selection proceedings. Federal Express obtained the ability as an incumbent carrier in the Japan market to go to an alternative, additional city—that is to say, a city other than Tokyo in Japan. They initially chose Nagoya, and they came to us some months ago and said that for a variety of reasons they had chosen not to start that service up. No one else in the U.S. all-cargo market has chosen as I understand it—I guess Northwest Airlines would be the only other eligible carrier, the only other all-cargo operator, incumbent all-cargo operator in the Japan market—no one else has chosen to take up that opportunity if I understand the situation correctly.

The other opportunity, of course, was UPS. The carrier selection proceeding concluded with UPS receiving that award. UPS plans to begin service beginning at the end of this month and, of course, the problem that UPS has in commencing that service at the moment is the unavailability of the slots that they need in the prime time evening hours to operate competitively. That is, indeed, the problem that we've already discussed which has required us to hold up the extension of the rights which the Japanese obtained in the same agreement.

Mr. **Oberstar**. In the underlying philosophy or principles, to use a less comprehensive word, the Japanese have followed a policy of strengthening the strong and not spreading their benefits to a multitude of carriers as we have done and as we had hoped would be the benefit of deregulation; there would be a multiplicity of carriers competing in the marketplace with a great benefit for consumers and opportunities for effective entrepreneurs.

The Japanese have followed a very careful strategy of strengthening the strong, building up JAL until it was dominant in the routes and markets that it served. Then they allowed another carrier. All Nippon Airways to come along on passenger service and NCA on cargo.

One very effective entrepreneur in the U.S. scene, Mr. Checchi of Northwest Airlines, has suggested that U.S. policy should not be to award six routes to six different carriers, but put more of our eggs in one basket. Focus more of the benefits to the carrier best able to compete with the foreign carriers. What's your reaction?

Mr. SHANE. I think Mr. Checchi is adopting a high risk strategy by suggesting a proposition like that, not knowing exactly whose basket all of our eggs would go into. I don't think that the United States ought to consider seriously shifting ground and concentrating the economic opportunities that we obtain in these bilateral agreements on a single carrier in any market. I think we have enjoyed enormous success. Again, the charts that are before you demonstrate the level of that success from the multiplicity of carriers and the strength that they all bring to the market.

Multiple designation has been part of our negotiating policy from the very beginning. We have something like eight airlines flying to France, and the market shares between U.S. carriers and the French carrier are so overwhelmingly in favor of the U.S. carriers that indeed it begins to complicate our relations with France. We have to think hard about how to strengthen Air France in that market in order to maintain healthy economic relations in aviation with the French. That's not a bad problem to have, Mr. Chairman, and I think we would not have that problem if we adopted the French policy and tried to put all of our eggs, if you will, in a single carrier's basket for services between the United States and France. It would hurt the U.S. carrier market share and, indeed, I think it would ultimately hurt U.S. communities that benefit from the more direct services they get from the multiplicity of carriers that we have in a market of that kind.

Mr. OBERSTAR. The underlying principle, though, is still very valid that whatever the number of carriers, we must negotiate rights for rights, values for values and enforce those rights to assure that the values will be played out.

Mr. SHANE. Absolutely.

Mr. OBERSTAR. Moving north to Canada, these are going to be the upcoming talks between the United States and Canada, between you and your counterpart, Mr. Lewis. They're going to be very significant talks, very benchmark perhaps in aviation trade kinds of talks. Canada very likely is interested in some form of cabotage, and I always get a little concerned about that. The U.S. market is so big that other countries smaller than us in population or in GNP say, well, you have the capacity in the United States to absorb our little carrier, our little piece of the marketplace. They do it in steel and they do it in VCRs, and they do it in color TV, now aviation. Just let us little folks come in and we're no big threat to the United States. Why don't you just let us have a little piece of your market. Tempting.

What would be the benefit to U.S. carriers of an agreement that envisions cabotage?

Mr. **Shane**. The simple answer to that question at the moment is that number one, of course, they would have access to the internal Canadian market which would be a net addition to their own domestic market in the United States and a net addition to their transborder markets. We need to work harder to calculate the precise economic benefit of that and that's, of course, something that will have to happen in the course of the negotiating process.

I would say a second benefit is out there as well, and that is that we need to find a formula that will at long last liberalize the transborder market generally. We need much better access to Canada for American communities and for American carriers. The kinds of connections that currently exist are an anachronism given the size of this market, the number of emplanements every year, and the pent-up demand for easier travel in U.S.-Canada city pairs.

The Canadian side sees this as a terribly important agreement as well, but they look at the United States as a market in which they cannot compete very effectively given the different geographical sizes of the two markets. What the Canadians have said to us is, we're prepared to sit down and figure out how we make the transborders market as flexible and as liberal as possible, thereby giving greater opportunities to communities and to travelers and to airlines on both sides of the border. But we're not prepared to do that unless we get something that you haven't been willing to talk to us about yet, and that is access to your internal market. Otherwise, that multiplicity of airlines that you have in the United States will dominate the transborder market to such an extent that the Canadian airlines will be non-entities in that market after some short period of time.

All we have said thus far is okay, if that's the basis upon which the Canadians are prepared to negotiate with us and if, indeed, it is the case that we ought not to be terribly worried about the possibility of Canadian carriers operating within our internal market given the size of our domestic airline industry and the size of the Canadian airline industry, then why not put cabotage on the table; why not at least leave it there as a proposition to be examined in the course of discussing how we can better improve, most effectively improve the transborder market?

I can't give you a definitive answer, Mr. Chairman, about the benefits that will flow to the United States carriers at the moment because we really haven't seen those benefits described to us yet. The negotiating process, it seems to me, is going to be a terribly important part of the process of trying to identify those benefits.

We're going to begin the process, I should say, before we ever sit down with our Canadian counterparts, by having internal discussions with all of our constituencies here in the United States. The first meeting I believe is to be held next Tuesday in the Department of Transportation. We expect to talk to labor, to our communities, to our carriers and to other interests to ensure that we understand all that we have at stake in these negotiations and to ensure that we are responding as effectively as we can to all of those interests. And, indeed, at the end of the day, given the fact that it is literally against the law for us to extend cabotage rights to a foreign carrier, Congress will ultimately have to decide whether or not to ratify any bilateral agreement that we present in a way that Congress normally does not have to do. There can't be an agreement with cabotage unless the Federal Aviation Act is amended.

So we see this as being a very important step forward. I think you've described it precisely the way I would describe it. It will be an important laboratory in which to discuss for the first time whether some of our traditional rules about international aviation deserve reexamination. That discussion will be in a context in which we understand the limits, or should at the end of the process, understand completely the limits of what we are extending and what we're doing.

Mr. OBERSTAR. Recognize in that context then—you've touched on the matter of labor issues—that current law bans foreign flight crews operating aboard U.S. aircraft on point-to-point service within the United States. Cabotage under some regime could change or result in a change or departure from that principle and would also have to be subject to legislative action by the Congress. Have you given that issue some thought?

Mr. SHANE. Oh, indeed.

Mr. OBERSTAR. Excuse me for interrupting, but I don't know what Canadian law is on that subject. I imagine they have the same protection for their labor.

Mr. SHANE. No, before we even thought about a joint announcement with Canada in which we would entertain a negotiation of the sort that we're talking about, I sat down with my colleagues in the FAA to review the variety of regulations that would have to be reexamined and, indeed, some of the statutory underpinnings of those regulations, just to get an understanding of the scope of what would have to be addressed. It seems to me that if we start getting close to an exchange of cabotage rights, then there will have to be a parallel consultation between the aeronautical authorities—that is to say, the FAA in the United States and their Canadian counterparts as well—because it seems to me that there are a whole host of rules that will have to be reexamined. You mentioned one.

Even if we established an agreement in which any time a Canadian aircraft came into the United States and then went on to a second point in the United States carrying local traffic, it would have to have a U.S. citizen crew, I believe that the FAA requirements would prohibit a U.S. citizen crew from flying that airplane. They may only fly U.S. registered aircraft in domestic markets. They can't fly a foreign registered aircraft. That would be a net addition, it seems to me, to the airplanes that the pilots could fly around the United States, but it would not be possible unless we began to reexamine some of the rules that currently apply.

Mr. OBERSTAR. Exactly. I think you'd have to consider some form of joint certification by Canada and the U.S. of U.S. and Canadian carrier pilots similar to the regulation of pilotage on vessels in the Great Lakes where you have the B licenses that permit under certain circumstances ship masters of foreign registry to navigate the

Great Lakes only after they have passed in effect an experience test. Where Canadian and U.S. pilotage rules are coordinated, you'd have to be taking another step there. Not only with respect to flight attendants, also the flight deck crew. I think there are a number of those issues that have to be thought through very, very carefully. Obviously you are aware of that and addressing it.

I suspect with the recent victory of the NDP in Ontario that labor voices are going to be raised very significantly with respect to this type of agreement since Ontario would be one of the major impact points.

But on the other hand, maybe we will be able to find some way of establishing non-stop service between Ottawa and Washington, D.C. The failure to have such is a blot on the record of aviation of both countries.

Mr. SHANE. That's right. Mr. Chairman, that particular route is just symbolic of what's wrong with the U.S.-Canadian aviation relationship today, and it's that kind of an anachronism that both sides are trying to get past.

Mr. OBERSTAR. We must briefly address route transfer policy. Does the Department have a policy of approval of route transfers that are privately negotiated among carriers or between carriers when it is determined that such are in the public interest?

Mr. SHANE. Well, the Federal Aviation Act itself contemplates that there cannot be a privately negotiated route transfer without Department of Transportation approval, and the Department of Transportation approval cannot be given unless it's found—the transfer is found to be in the public interest. That is another way of saying that the Federal Aviation Act appears to contemplate that such transfers occasionally can be approved by the Department of Transportation.

I would say our policy is very much a case-by-case policy. If the public interest does seem to be served by a particular transfer, then we would approve it and, indeed, we have approved many on that basis. On the other hand, where there appear to be impediments to the public interest, if opening a route to a broader competition among carriers would seem to hold the promise of better service for the public, then we have that option as well, although typically if you hold that possibility out to the participants in a proposed route transfer, then I suppose the route transfer transaction would go away. You would have then an incumbent operating the route, and I imagine the incumbent would want to keep operating the route.

So what you're doing in effect by saying we'd rather see who else is out there to operate this route, you're basically saying there won't be a route transfer; you're just disapproving it and you're keeping the incumbent in place.

Mr. OBERSTAR. Is that the sort of thinking that has held up the TWA transfer of the Chicago-London route?

Mr. SHANE. I hope you'll forgive me, Mr. Chairman, but my general counsel would cut my head off if I offered any substantive comment on what was going on in the Department of Transportation on a pending proceeding.

Mr. OBERSTAR. Suffice it to say, it's still under review?

Mr. SHANE. Correct.

Mr. **Oberstar**. I'm very pleased with your attention to the many outstanding issues, the questions of capacity in Europe, their slot availability, the inadequacies of the air traffic control system in Europe as they affect our negotiations. I'm very pleased with what I see as a wide ranging understanding of and sensitivity to these issues and a willingness furthermore to address them head on.

I know that there will be many other questions raised by the many interested parties, and we will take those questions, hear their concerns at subsequent hearings. For the moment, thank you very much for spending a very long morning with us and for sharing your thoughts on the state of the art of cargo and passenger trade in the Pacific and in the Atlantic and in the North and South America regimes as well.

Mr. **Shane**. I've enjoyed it, Mr. Chairman. Thank you very much.

[The prepared statement of Mr. Shane follows:]

STATEMENT OF JEFFREY N. SHANE
ASSISTANT SECRETARY FOR POLICY AND INTERNATIONAL AFFAIRS
U.S. DEPARTMENT OF TRANSPORTATION
BEFORE THE
HOUSE PUBLIC WORKS AND TRANSPORTATION COMMITTEE,
SUBCOMMITTEE ON AVIATION
OCTOBER 11, 1990

Mr. Chairman, Members of the Subcommittee, I appreciate this opportunity to meet with the committee to outline major recent developments in international aviation and indicate the direction in which we are moving to increase opportunities in this important sector of our economy.

We have been actively pursuing international aviation policies designed to expand the service options and economic benefits both for the traveling public and communities that receive service and for our aviation industry that provides it.

We are achieving very positive results from these efforts, and I am pleased to report that U.S. cities and U.S. airlines are doing very well. In 1989, approximately 550 international nonstop combination services were operated to U.S. cities. Of these, 115 or 20% did not operate in 1984. Over this same period, ten (10) U.S. cities received first time international air service.

Our airline industry has benefited substantially from the growth and expansion of the international aviation market. In 1989, U.S. airlines carried more international passengers and more international freight than the airlines of any other nation. The U.S. airline share of worldwide international traffic has risen during the past three years, reversing an earlier trend, and is now over 20% of the worldwide total. As another measure of the improvement of U.S. carrier position in the international market, U.S. carriers have been increasing their share of international passengers to and from the United States, now carrying 52% of that group, up from 48% in 1985. Moreover, for the period 1984 through 1989, the passenger traffic growth rate of U.S. airlines has surpassed that of foreign flag airlines in each major world region. In the U.S.-Asia/Pacific market, the most rapidly expanding market, U.S. carriers experienced a 106% growth in passenger traffic compared to 56% growth for foreign flag carriers. In the U.S.-Europe market, the comparable numbers are 56% for U.S. carriers and 44% for foreign carriers. In the U.S.-Latin America market, they are 42% for U.S. carriers and 27% for foreign flag carriers.

International cargo operations have shown a similar growth trend. Between 1984 and 1989, the percentage of international scheduled freight traffic carried by U.S. airlines rose from 13% to 16.7%, a remarkable 30% increase in market share.

Charts reflecting these developments are attached to my statement.

AVIATION NEGOTIATION POLICY INITIATIVES

Although we are pleased with the growth of international air service in recent years, we believe that greater progress can be made. A major problem is that the current system of bilateral air agreements still relies to a large extent on government regulation of air services. In our view, this inhibits the achievement of the potential economic benefits that both the United States and foreign countries would derive from a competitive, market-driven air transportation regime. We have recognized this problem and have taken initiatives to address it.

To further expand international aviation service opportunities, the Department, under Secretary Skinner, has pursued a progressive aviation negotiation policy by proposing "open skies" aviation agreements with several of our most important aviation partners. Such agreements would grant the flag carriers of these countries and of the U.S. full access to points in the other country and would remove essentially all economic regulatory restrictions on the operation of airline services. This would give carriers freedom to price their services in response to marketplace conditions and provide benefits to air travelers and shippers by reducing the cost of air travel and expanding service options. Based on experience over the past decade, we know that the U.S. economy would derive a significant overall benefit from new services stemming from such agreements. We have proposed "Open

Skies" agreements to Germany, the United Kingdom, France and Canada.

As expected, the idea of "open skies" is appealing to some countries, but they are reluctant to move into an aviation environment that places full reliance on competitive market forces.

This situation reflects the strength of U.S. carriers and further highlights the success of domestic regulation.

Deregulation created an environment which required carriers to compete, and through competition, to become innovative, responsive to the marketplace, and more efficient. Today, there is no question that the U.S. air transportation system is the most efficient in the world and that U.S. airlines are the world leaders in just about every measurement.

The success of our deregulation has spurred many countries into liberalizing their aviation environments. We remain hopeful that more countries will come to appreciate that open markets produce enormous economic dividends, and, therefore, join us in eliminating the restrictions on international operations which prevent those benefits from being fully realized.

With these considerations in mind, we have taken a number of important steps, both in revising bilateral agreements and in introducing unilateral initiatives, to advance our quest for a freer, more competitive international air transportation system. We believe that these developments have been extremely important both in terms of improving air service in discrete markets and in moving international aviation toward our overall objective.

SPECIFIC BILATERAL NEGOTIATIONS

Canada

At the moment, some of the most exciting prospects are with Canada, our largest aviation partner. Last week, Secretary Skinner and Canadian Transport Minister Doug Lewis announced that the two countries would begin negotiations to create an open aviation market that would dramatically expand air service between the two countries. They hope to achieve an open regime that would permit all types of air service between any cities in the two countries by all U.S. and Canadian airlines. A liberal open skies agreement would make available substantially more service to many cities for air passengers and shippers and generate billions of dollars in economic benefits for U.S. airlines and U.S. cities. We intend to work hard to reach an agreement and realize the substantial potential benefits from this proposal.

Germany

In 1989, we began negotiations with Germany -- our fifth largest international aviation partner -- on expanding opportunities for both countries. Our key objective is to reach an agreement that would give airlines the maximum degree of flexibility to exercise their managerial discretion in determining what services to provide. A primary goal is to achieve a more liberal pricing environment, a feature that concerns the Germans. The German Government would prefer to continue to have discretion in approving prices for travel originating in Germany. We, however, are disturbed that the German authorities continue to disapprove U.S. carrier fare initiatives even when such fares are comparable to approved fares in the market. These fare disapproval actions appear to be taken to protect Lufthansa, a German flag carrier. We hope to convince the German Government that the disapproval of U.S. carrier low-fare initiatives has harmed German travellers by denying them the benefits of low air prices. We plan to seek a resumption of our negotiations in the near future, and we are prepared to consider appropriate phasing mechanisms to address German concerns if the end result is an "open skies" agreement that gives airlines of both sides maximum freedom to operate.

Japan

Also in 1989, we concluded a new agreement with Japan, our third largest aviation market, that represents the most dramatic expansion of service since the original bilateral agreement was signed in 1952. The agreement gives the U.S. the right to award three new combination services from the U.S. to Tokyo, three new combination services from the U.S. to points other than Tokyo or Osaka, and one new all-cargo route to Tokyo. It also increases the number of U.S.-Japan charter flights permitted for U.S. carriers by 50%, from 300 to 450. The agreement gives Japanese carriers the right to operate six new services from Japan to U.S. cities, expands Guam/Saipan-Japan services and expands the number of charter flights permitted for Japanese carriers. We are currently implementing this agreement.

Although we have made substantial progress in expanding aviation opportunities with Japan, congestion at Japanese airports, particularly at Tokyo's Narita airport, continues to be a major obstacle to opening up the Japanese market. A current problem has arisen from the Department's recent award of authority to UPS to operate an all-cargo service to Tokyo under the terms of the 1989 MOU. UPS requested evening departure slots at Narita that would enable it to compete with other cargo carriers in the market. They were granted morning departure slots for three days and were told that no slots were available for a Saturday departure. We believe that UPS is correct in its assessment that it cannot compete effectively without evening departures. Until this issue is resolved satisfactorily, we are withholding the issuance of authority to JAL and NCA, two Japanese carriers that seek to implement all-cargo services to Chicago under the 1989 MOU.

Mexico

As with Japan, we have recently increased air service with Mexico, our fourth largest international aviation market, as the result of a more expansive bilateral air transportation agreement. That agreement increased the number of combination service routes between the two countries, secured the right for designation of two carriers on some routes, provided for the first scheduled all-cargo service, and created a more positive environment for charters.

United Kingdom

We have also made some incremental progress in expanding the U.S.-U.K. air transportation market, which is the second largest U.S. international passenger market. In an agreement reached earlier this year, we gained three additional opportunities for U.S. airlines to serve U.K. cities other than London. Continuing growth in this market has been achieved despite the fact that, at British insistence, the U.S.-U.K. bilateral aviation agreement remains among our most restrictive, with limits on gateways and designations and government oversight of fares and schedules. In addition to the limitations on operating rights contained in the bilateral aviation agreement, we also have several serious "doing business" problems with the British. The user charges imposed on U.S. airlines at London's Heathrow Airport are, we believe, excessively high and inequitably allocated. Since we were unable to resolve this issue through the negotiating process, the United

States is currently involved in an arbitration with the British on this problem. We are also looking into a complaint filed by American Airlines under the International Air Transportation Fair Competitive Practices Act concerning that airline's inability to handle the check-in of its passengers with its own personnel at London's Gatwick Airport. Given the importance of this aviation market, we are committed to exploring with the British the prospects for a broad-based liberalization of this relationship.

CITIES PROGRAM

In January of this year, the Department implemented its new "Cities Program." This initiative responds to requests by many communities for relief from a serious flaw in the bilateral system. Under that system, a U.S. community may lack service because U.S. carriers have decided not to provide it, although authorized by the bilateral, and because foreign air carriers, although willing to provide it, are not authorized to do so by the bilateral. To correct this problem, our cities program grants foreign airlines authority to operate extra-bilateral services to U.S. cities under certain well-defined circumstances. These circumstances have been carefully developed to strike a sound balance between the need for improved international service and the need to maintain an strong and competitive U.S. carrier industry. Thus, to quality for program authority, there must be a procompetitive agreement between the United States and the country of the foreign flag carrier, and there cannot be nonstop or one-stop single-plan service between the U.S. community and the foreign country. Other conditions are designed to insure that these important program objectives are met. Under the Cities Program, we have granted KLM authority between Amsterdam and Baltimore, Ladeco between Santiago and Washington; Lufthansa between Frankfurt and Charlotte; and Swissair between Zurich and Philadelphia.

Please note that the Cities Program is intended to supplement the aviation agreement process and not replace it. This is important because, in the current environment, we must continue to rely on that process to provide the most comprehensive benefits. As a result, we have continued to aggressively pursue the goals of opening up markets and removing restrictions on operations through the negotiating process.

MULTILATERAL NEGOTIATIONS

We are also considering alternatives to the bilateral negotiating process.

As you are aware, the European Community (EC) plans to form a single aviation market. This presents both opportunities and problems, with both the Community's developing external aviation policy and its internal aviation legislation.

There is an apparent consensus within the EC that it will eventually establish a common external policy and a coordinated negotiating approach to outside countries. However, the precise shape and timing of the external policy are far from settled, and the Commission's proposal for unified EC aviation negotiations is highly controversial within the Community.

Multilateral negotiations with the EC could offer a great opportunity to liberalize aviation services, because the Community could bring much more to the negotiating table than any one of its 12 members, each of whose home markets are much smaller than ours. We hope that the EC will resolve the economic and political issues involved in establishing a common negotiating front in a way that will promote broader exchanges of market opportunities.

In the meantime, we have insisted, and have been assured, that our existing bilateral agreements with EC member countries, including intra-European fifth freedom rights, will be respected. However, the Commission's view of intra-European fifth freedom rights as a "Community asset" for negotiating purposes has complicated some bilateral negotiations.

The Community's internal market aviation legislation offers the opportunity to remove regulatory barriers and to achieve greater efficiencies to the benefit of both airlines and users. However, that opportunity will be lost if instead of reducing regulation, its enforcement is merely transferred to Brussels. We have also been closely monitoring the Commission proposals to ensure that U.S. airlines operating within the EC, as well as on U.S.-EC routes, are treated fairly in areas such as CRS, airport slot allocation, and pricing rules.

We have a good working relationship with the Community on all levels, and we have had discussions on many aspects of EC aviation policy to register our concerns and resolve potential problems. As the EC moves closer to completing its internal market program and establishing a common external policy, we expect to extend these relationships and contacts to promote competition and ensure that U.S. interests are respected.

OTHER INTERNATIONAL AVIATION POLICY ISSUES

I would like to address a number of other important issues concerning international aviation policy.

Airline Citizenship Issues

The 1980's were characterized by an accelerating trend toward globalization of the industry. Airlines worldwide have made numerous linkages to put themselves into new and better competitive positions for the future. These linkages include multinational investments and cross-investments in airline companies, marketing agreements, and development of multi-carrier ownership of computer reservation systems.

Many of the world's largest airlines now have significant ties to one another. For example, KLM and British Airways each own 20% of Sabena. Air New Zealand is owned by a group including Qantas, Japan Air Lines and American Airlines. Delta and SwissAir own 5% of each other's stock. The GALILEO computer reservation system was formed by KLM, British Airways, Swissair, Alitalia and Covia. The competing system—AMADEUS was formed by Lufthansa, Air France, Iberia, SAS and Texas Air.

International investment and cooperative activities can lead to better, more competitive service for the consumer and greater economic efficiency. International sources can provide much-needed new capital for our airlines thereby providing for new entry, more competitive markets and greater employment in the industry. Cooperative arrangements can bring new managerial and technological innovation thereby improving our carriers' competitive position. As a nation, we cannot afford to forgo these benefits, and therefore we encourage these developments. But we do so within the limits of our law.

Therefore, the Department is promoting a strong and competitive U.S. airline industry in this evolving global environment, while at the same time ensuring adherence to the statutory requirement that U.S. air carriers meet certain citizenship standards. These standards include, in particular, that U.S. air carriers be citizens of the United States, as defined by the Federal Aviation

Act, and that U.S. air carriers actually be controlled by U.S. citizens.

Two cases illustrate our approach to foreign investment in U.S. carriers.

Last year, we reviewed a transaction where Wings Holdings, a company formed by Alfred Checchi, purchased the parent of Northwest Airlines. The record showed that Wings relied heavily on foreign investment to finance the purchase. One foreign investor, Elders Ltd., bought $80 million worth of common and preferred stock in Wings, including 15% of its voting common. Another foreign investor, KLM, supplied more than half of the equity invested in Wings through large holdings of nonvoting common and preferred shares.

The Department found that Elders' investment would make a positive contribution to the transaction without raising issues of control. On the other hand, the Department was concerned that KLM's large stake in Wings, together with other links between KLM and Wings, would lead to foreign control of Northwest. In this context, the Department took decisive action to assure continued U.S. control of Northwest and entered into a consent agreement with the carrier and Wings to achieve that objective. I am satisfied that these actions have been successful and that Northwest remains firmly under U.S. control.

Recently, the Department had to consider the citizenship issue with respect to Scandinavian Airlines System's (SAS) acquisition of an 18% voting interest in Continental Airlines Holdings. Although SAS will be the largest shareholder, we are convinced, after a careful examination of the arrangement, that SAS will not be in a position to control Continental. Our decision on this issue was reached, in part, based on facts demonstrating that the transaction had been carefully structured to ensure the independence of Holdings's Board of Directors.

Unfair Competitive Practices

Another area affecting international aviation that the Department is actively involved in is ensuring that foreign governments and foreign carriers allow U.S. carriers to fully exercise their aviation agreement rights and that carriers can compete on a fair and equal basis.

In 1979, Congress, in the International Air Transportation Competition Act (IATCA), amended the Federal Aviation Act of 1958 and the International Air Transportation Fair Competitive Practices Act of 1974 (IATFCPA) in order to increase the effectiveness of United States efforts to combat unfair, restrictive and discriminatory practices of foreign governments and foreign air carriers. Under these provisions, the Department is empowered to take swift retaliatory action against foreign anticompetitive practices.

Generally speaking, unfair competitive practices have involved denial of, or restrictions on, operating rights or fares in violation of a bilateral air transport agreement. They may also involve unfair competitive practices involving air carrier operations.

Since our objective is to resolve unfair competitive practice problems as quickly and painlessly as possible, we often seek to find a negotiated solution before taking sanctions. Our experience is that such complaints are usually resolved through intergovernmental consultations or by intercarrier negotiations encouraged by the IATFCPA process. Recognizing the importance of ensuring a fair, competitive environment for our carriers to operate in, we have been diligent in processing IATFCPA complaints and in using the powers conveyed to us to ensure that U.S. airlines are not disadvantaged.

Over the past five years, the Department has acted on ten complaints. Three of these involved discriminatory practices against U.S. carriers in connection with computer reservation systems; five involved the withholding of operating rights guaranteed to U.S. carriers under bilateral agreement or other intergovernmental understandings; and two involved currency remittance problems.

Airport Slot Constraints

When our carriers face constraints on the availability of facilities that limit their ability to respond to market conditions, our goal is to make sure that they have a fair and equal opportunity to compete. One area of particular concern in this regard is the limited availability of landing slots at major international airports.

Recognizing the need for carriers to have access to airports at times that will enable them to compete effectively with one another, our policy is to try to make available to carriers slots at times they want. With the limited exception of Canadian services from La Guardia, the U.S. has only two slot-controlled airports with international operations -- O'Hare and Kennedy. At O'Hare, we provide slots for all international operations within two hours of the time requested. At Kennedy, meeting our international obligations is one of the criteria used in determining the hour that a slot is granted. Thus, while we have no similar two-hour rule, we do meet requests as closely as possible. By trying to meet all carriers' slot needs, we have set an example to encourage entry and competition in international aviation markets and to recognize that international obligations to provide access for carriers must be met.

We have encountered difficulties with our carriers obtaining landing slots at certain foreign airports, notably Tokyo. In some cases, it has been necessary to discuss the problems of carrier access with foreign governments and to reach agreements on steps to be taken to meet the demands of carriers. However, U.S. policy on international slots is not a one-way street. Our slot rule contains a reciprocity clause which permits the withholding of a slot from a foreign airline whose government does not provide comparable treatment. Although we have never had to use this provision, we are prepared to do so to ensure fair treatment for all carriers.

Aviation Security

Another area involving international air transportation that we are working hard on is aviation security. As you know, we have been carefully considering the recommendations of the President's Commission on Aviation Security and Terrorism since its report was issued in May. We are in the process of implementing most of the recommendations contained in the report, and I know that the subcommittee is familiar with our efforts in this regard.

We are particularly pleased with the performance of our civil aviation security liaison offices in Europe. We have a few more inspectors and liaison officers to place in Europe and the Middle East, and we have begun the process of placing people in Latin American and Asia. Along with these placements will come improved cooperation and better communication with our air carriers and foreign governments.

The Thermal Neutron Analysis (TNA) device in London at Gatwick Airport has been performing well and is producing a different kind of operational data which can be compared to the information we are gathering from machines at JFK, Miami and Dallas. We are progressing in our efforts to have a TNA placed at the airport in Frankfurt, and we are planning to place an additional machine at another location in Europe.

Let me assure you that the Secretary and the Administrator of the FAA place the highest priority upon our improving international aviation security and we will all be actively supporting these efforts by working closely with Vice Admiral Robbins and his staff in the new Office of Intelligence and Security.

Montreal Protocols

As a final issue, I would like to review the status of the proposed Montreal Protocols that would amend the passenger liability provisions of the Warsaw Convention.

The Warsaw Convention currently limits air carrier liability for passengers killed or injured in international air accidents to $75,000. The average recovery for passengers deaths in aircraft accidents not covered by the Warsaw Convention now exceeds $800,000.

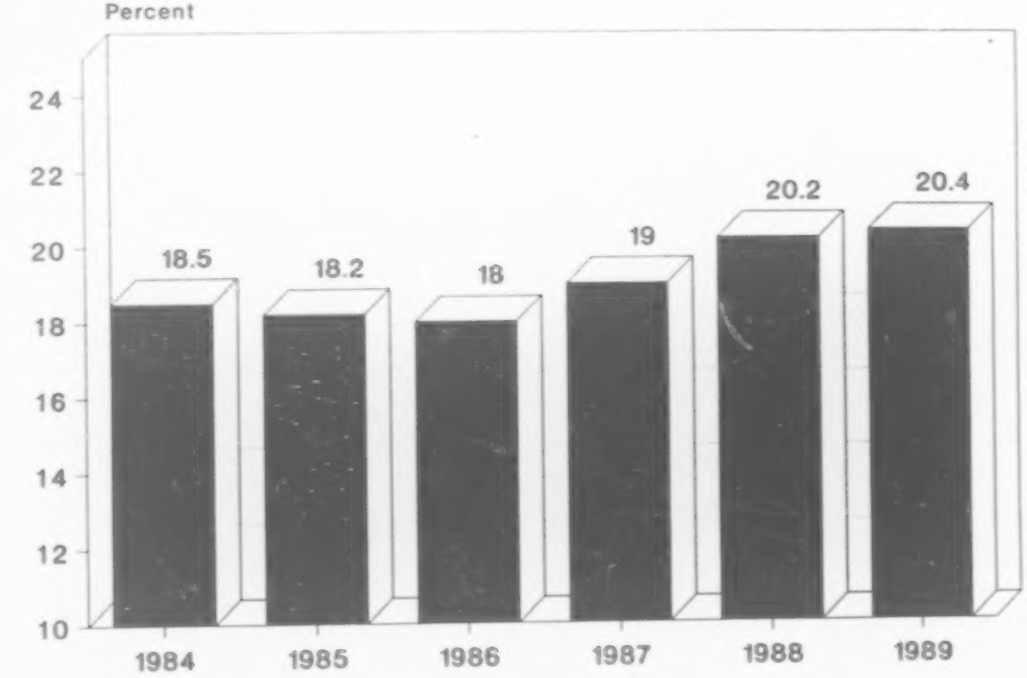
Currently pending before the Senate is a proposal to ratify the Montreal Protocols, coupled with a Supplemental Compensation Plan, which would provide for unlimited per passenger recoveries in international air transportation.

In June, the Senate Foreign Relations Committee voted to recommend Senate advice and consent to ratification of the Protocols with the supplemental plan, and we hope that the plan will be voted on by the Senate soon.

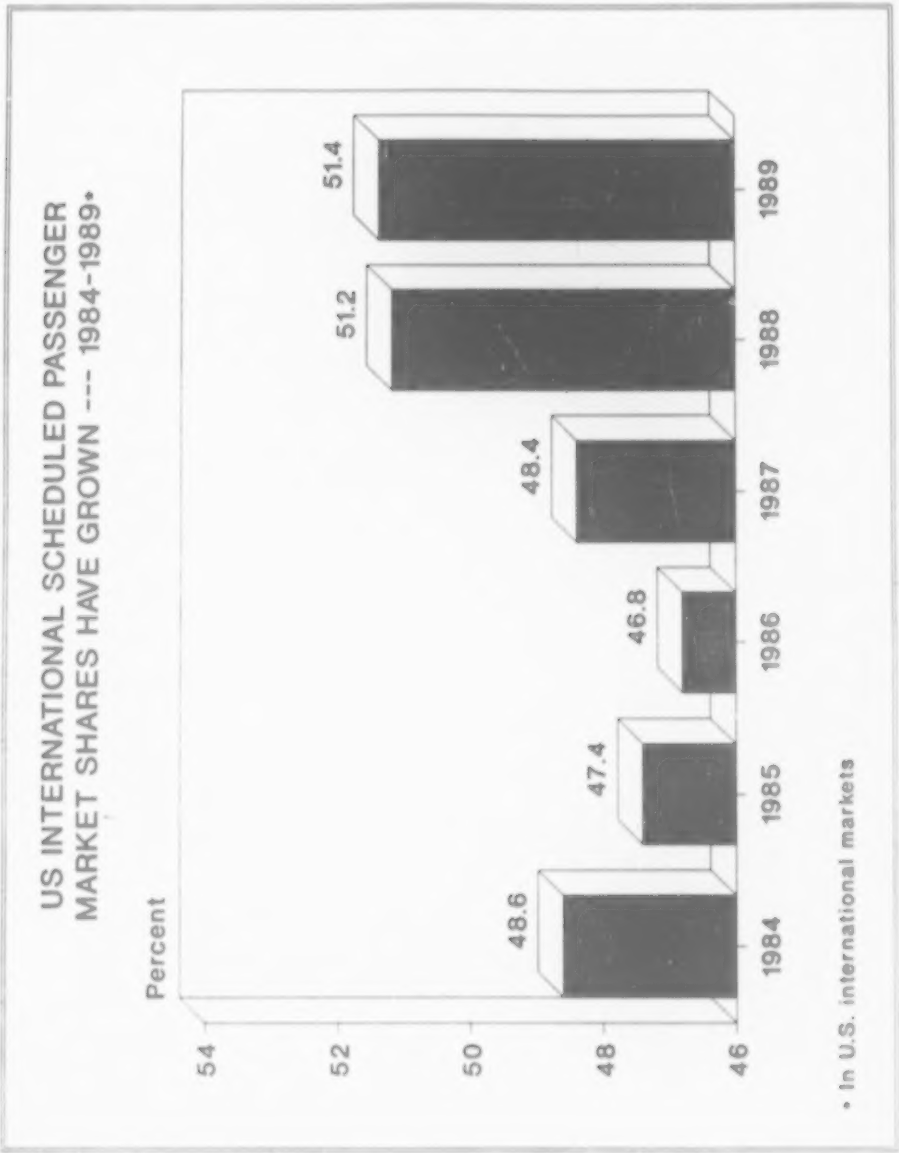
We consider ratification to be very important in order to provide fair liability coverage for U.S. citizens, ensure prompt and sufficient settlements of claims, reduce litigation, and provide for full recovery for U.S. citizens on flights between foreign countries.

I hope my testimony has been helpful in apprising the subcommittee of the extensive work that we are doing on international aviation issues. I am prepared to answer any questions that you may have.

US FLAG SHARE OF WORLD INTERNATIONAL PASSENGER TRAFFIC HAS GROWN---1984-1989•

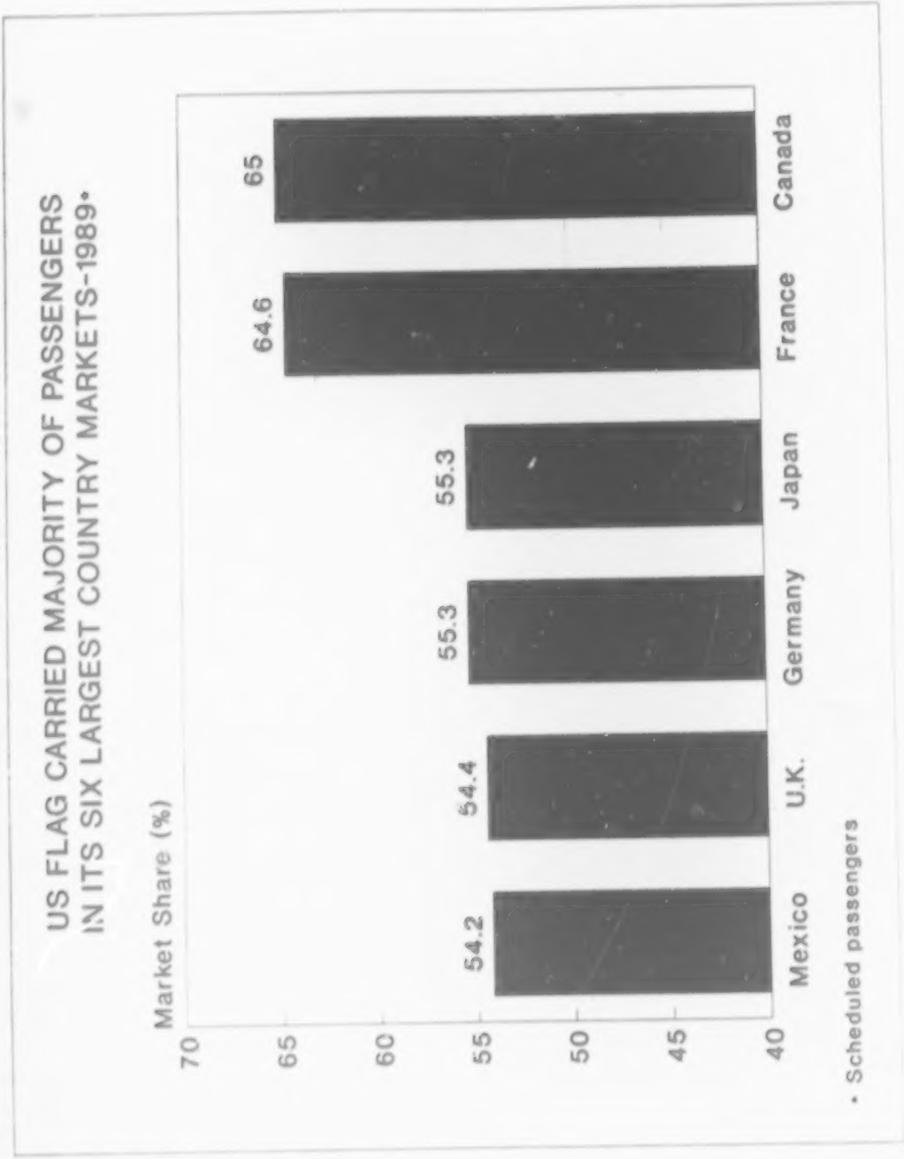


•US share of worldwide scheduled RPMs



US INTERNATIONAL SCHEDULED PASSENGER MARKET SHARES HAVE GROWN --- 1984-1989*

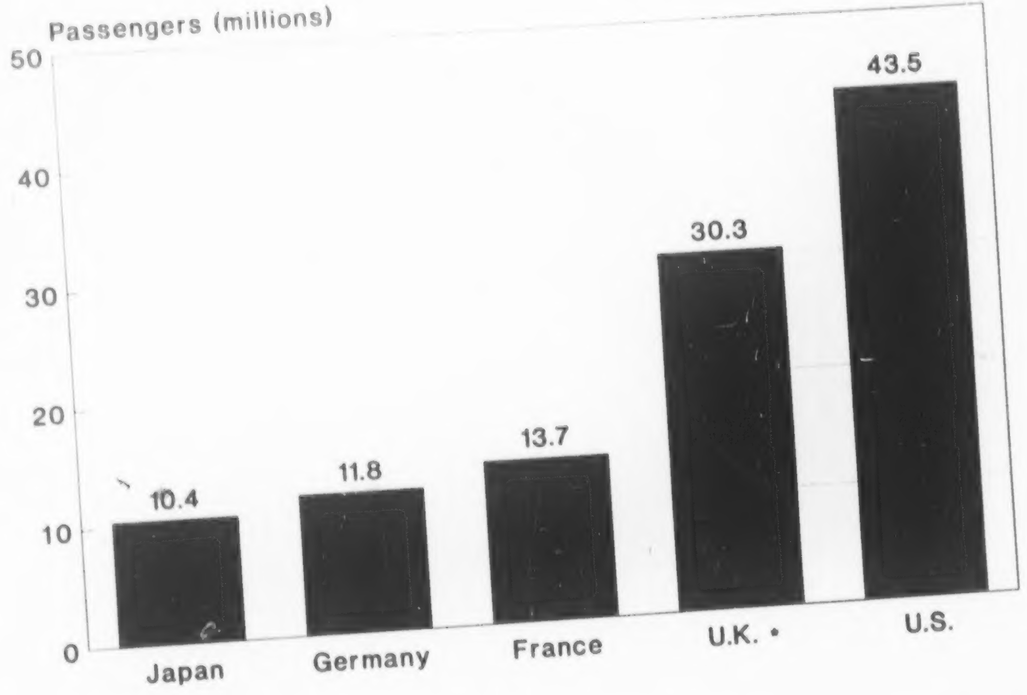
* In U.S. international markets



US FLAG CARRIED MAJORITY OF PASSENGERS IN ITS SIX LARGEST COUNTRY MARKETS-1989*

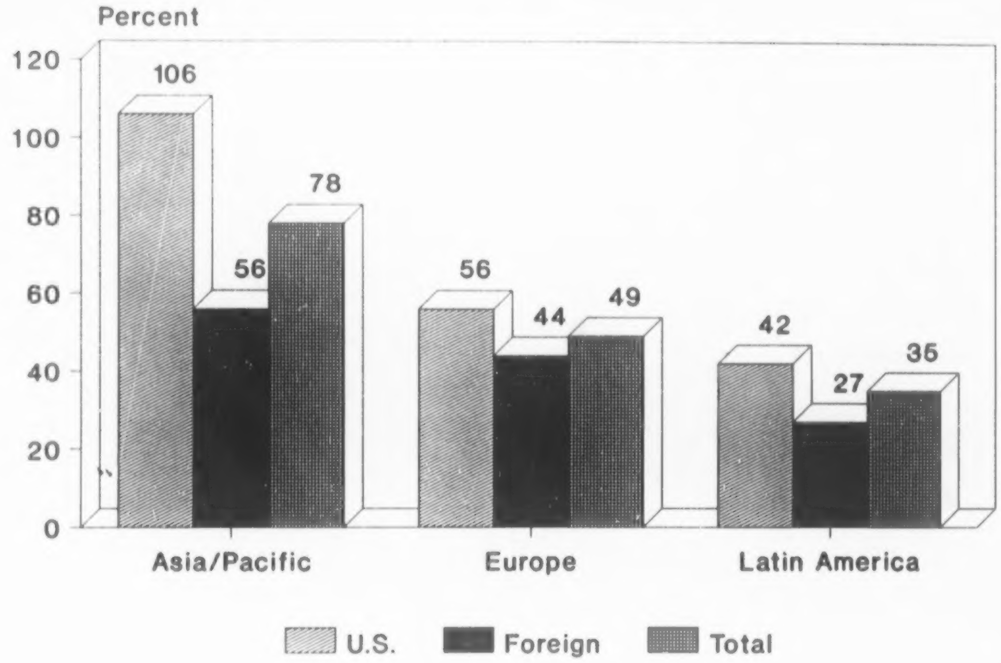
* Scheduled passengers

US FLAG RANKED FIRST IN TRANSPORT OF
INTERNATIONAL SCHEDULED PASSENGERS-1989

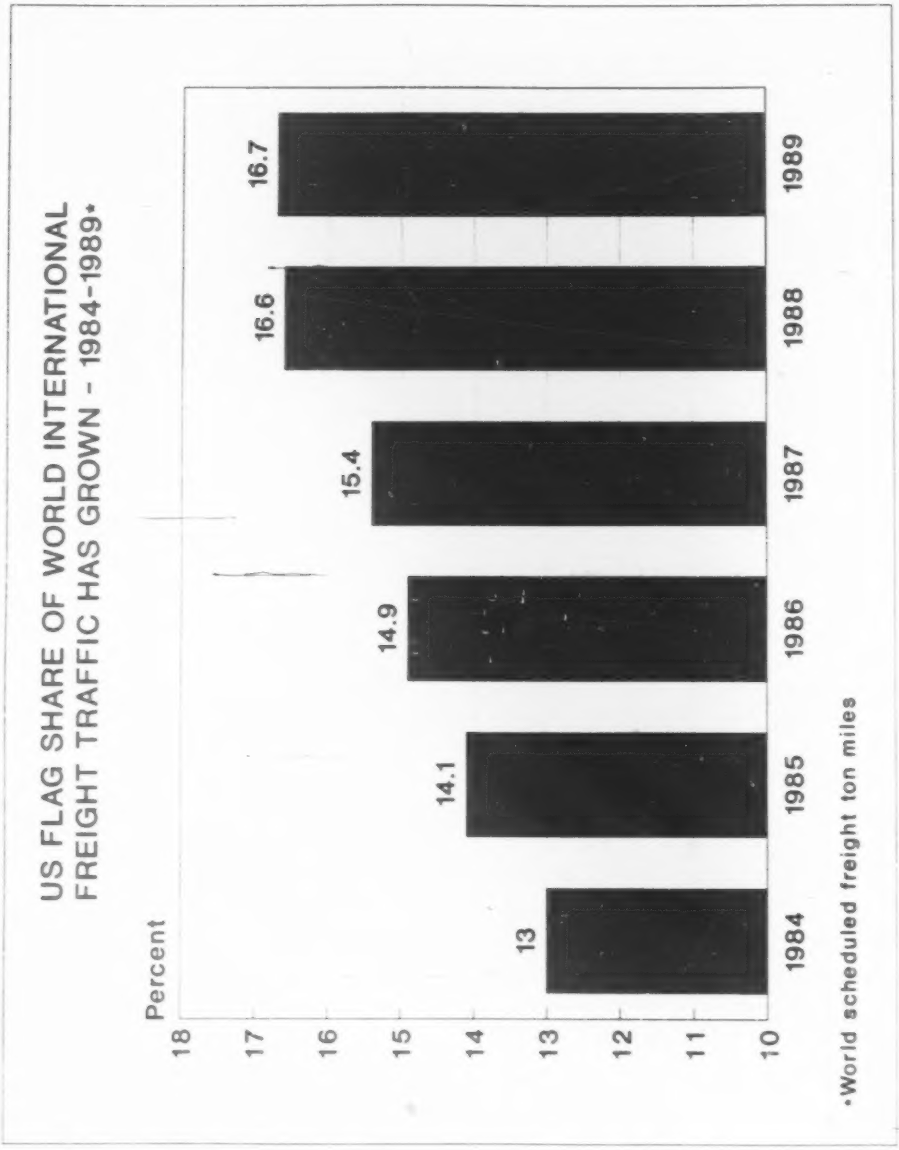


• Includes Hong Kong

US FLAG PASSENGER GROWTH HAS SURPASSED FOREIGN FLAGS IN MAJOR REGIONS 1989/84•

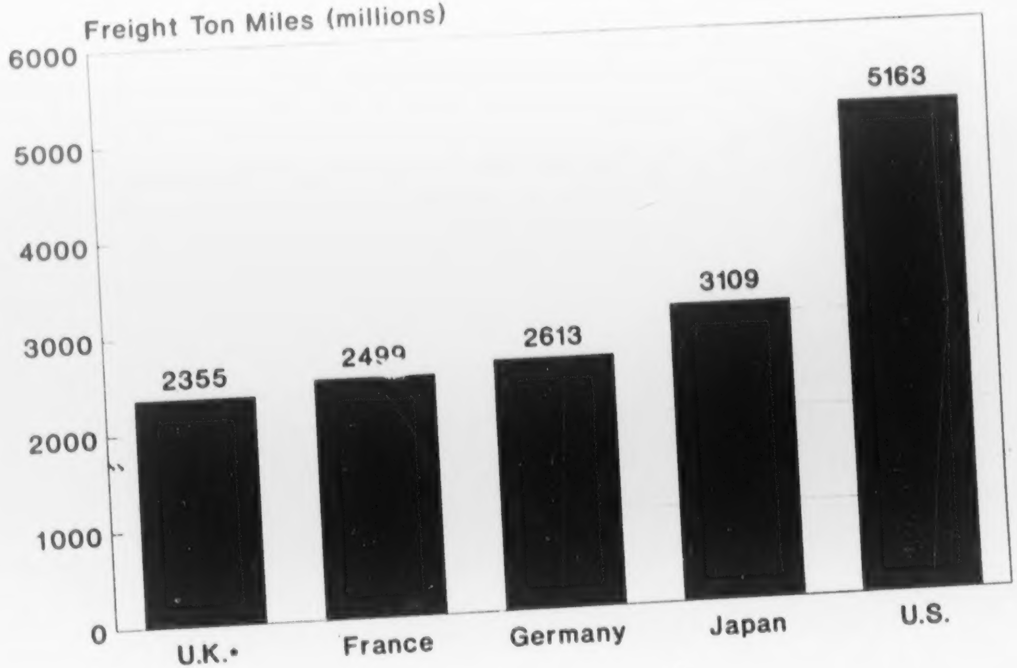


• In U.S. scheduled passenger markets



US FLAG SHARE OF WORLD INTERNATIONAL FREIGHT TRAFFIC HAS GROWN - 1984-1989*

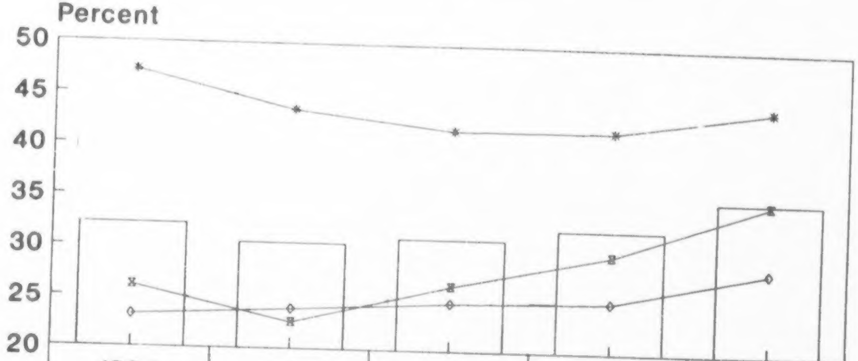
*World scheduled freight ton miles



US FLAG RANKED FIRST IN TRANSPORT OF INTERNATIONAL SCHEDULED FREIGHT - 1989*

* Includes Hong Kong

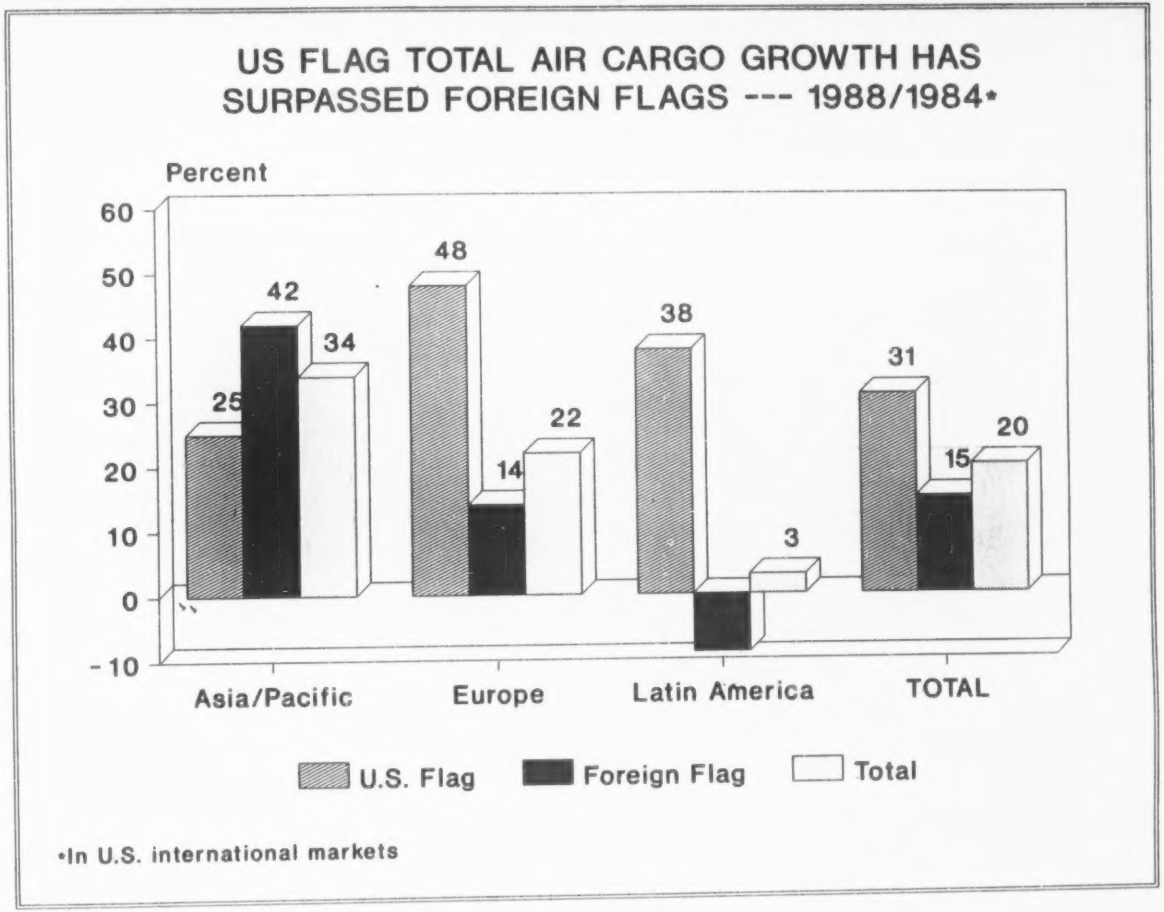
US FLAG INTERNATIONAL AIR CARGO MARKET SHARES --- 1984-1988*



	1984	1985	1986	1987	1988
Europe	23.2	23.9	24.7	25	28.2
Latin	26.1	22.6	26.4	29.6	34.9
Asia/Pacific	47.2	43.5	41.7	41.8	44.1
TOTAL	32.2	30.4	31	32.1	35.1

—◇— Europe —⌗— Latin —✱— Asia/Pacific ☐ TOTAL

*In U.S. international markets



US FLAG TOTAL AIR CARGO GROWTH HAS SURPASSED FOREIGN FLAGS --- 1988/1984*

*In U.S. international markets

Mr. **Oberstar**. The Subcommittee stands adjourned.

[Whereupon, at 12:35 p.m., the subcommittee was adjourned, to reconvene at the call of the Chair.]

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